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REPORT
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RURAL ELECTRIFICATION AND TELEPHONE REVOLVING FUND SELF-SUFFICIENCY ACT OF 1984

JUNE 29 (legislative day, JUNE 25), 1984.—Ordered to be printed

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Mr. HELMS, from the Committee on Agriculture, Nutrition, and Forestry, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany S. 1300]

The Committee on Agriculture, Nutrition, and Forestry, to which was referred the bill (S. 1300) to amend the Rural Electrification Act of 1936 to ensure the continued financial integrity of the Rural Electrification and Telephone Revolving Fund, and for other purposes, having considered the same, reports favorably thereon with an amendment and recommends that the bill, as amended, do pass.

SHORT EXPLANATION

The bill, as amended by the Committee, would amend the Rural Electrification Act of 1936 for the purpose of improving the financial condition of the Rural Electrification and Telephone Revolving Fund and making other changes in the rural electrification and telephone loan programs administered by the Rural Electrification Administration. Specifically, the bill:

(1) Revises the definition of the term "telephone service" (i) to specifically include the transmission of "data", and (ii) to include transmissions by wire, fiber, radio, light, or other visual or electromagnetic means, in addition to electricity;

(2) Expands the definition of the term "rural area" for telephone financing purposes by including areas not within the boundaries of cities, villages, or boroughs with populations of

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more than 2,500 inhabitants, instead of the present limit of 1,500;

(3) Converts certain long-term notes to revolving fund equity capital, rather than leaving them in their current status as liabilities of the revolving fund;

(4) Provides for two separate accounts within the revolving fund, one for the electric loan program and one for the telephone loan program, with assets in each account to be used only in connection with the operation of that account's program;

(5) Authorizes the Administrator of the Rural Electrification Administration, after obtaining the prior approval of the President of the Federal Financing Bank, to repurchase, without penalty, any outstanding certificate of benefical ownership having a remaining term of 7 years or more, when the rate of interest on the certificate of beneficial ownership exceeds the current rate on new certificates by at least 1 percentage point;

(6) Authorizes the lender of a loan guaranteed by REA, at the request of the borrower, to adjust without penalty the rate of interest on any advance having a remaining term of 7 or more years if the rate of interest exceeds the current rate on new advances by at least 1 percentage point. Any such adjustment may not be made more often than every 7 years;

(7) Eliminates the current statutory "standard" rate of interest of 5 percent for the electric and telephone loan program and requires instead that the Administrator establish a "standard" rate for each of the two accounts in the program, not less than 5 percent, that will produce anticipated interest income (including any appropriated funds and interest income from outstanding loans) equal to the amount of anticipated interest expense on all outstanding obligations of that account;

(8) Expands the eligibility criteria for "special" rate loans for electric and telephone borrowers, sets the rate of interest on such loans at not less than 2 percent (the current statutory requirement) nor more than one-half the "standard" rate, and makes such loans mandatory, rather than discretionary;

(9) Requires the Administrator to establish a reserve in each of the two accounts to be use to cover the cost of loans made at the "special" rate of interest and requires the Administrator to put into each reserve, annually, an amount equal to 1 percent of the payments of principal and interest made during the preceding fiscal year. If either reserve is not adequate to cover the cost of the "special" rate loan program, the Secretary of Agriculture must include, in his next budget request, a request for funds to cover the residual cost;

(10) Requires the Administrator, for the purpose of assisting borrowers in improving their financial condition, to guarantee loans made by any lender approved by him (in addition to any legally organized leading agency) for any purpose provided in the Act and for refinancing assistance.

(11) Requires the Administrator to accommodate or subordinate liens or mortgages at the request of the borrower for any purposes that would improve the efficiency, effectiveness, or financial stability of the borrower, upon a finding that the bor-

rower has, or will have, the ability to repay its existing and proposed indebtedness;

(12) Provides that the loan criteria and ratios for supplemental financing for insured electrfication loans that were in effect as of July 15, 1982, will be maintained in any fiscal year in which the minimum electrification loan level is established by law at less than $1 billion;

(13) In the case of a cooperative borrower located in a noncontiguous State not served by a statewide or miltistate power grid, requires the Administrator to apply the same minimum financial standards separately to the distribution assets and to the generation and transmission assets of the cooperative as are separately applied to cooperatives classifed as either a distribution or a generation and transmission cooperative;

(14) Deletes the termination date of fiscal year 1991 on the obligation of the United States to purchase Rural Telephone Bank capital stock;

(15) Eliminates the requirements (i) that the Secretary of Agriculture approve certain loans made by the Rural Telephone Bank for the acquisition of telephone lines, facilities, or systems, (ii) that the location and type of such lines, facilities, and systems will improve the efficiency or financial stability of the borrower's system, and (iii) that, in the case of acquisitions of exchange facilities for local telephone service, the size of the system to be acquired cannot exceed the size of the borrower's system as it existed at the time of the borrower's first loan from the Telephone Bank;

(16) Eliminates the prohibition against the making of telephone loans by the Administrator or the Rural Telephone Bank unless (i) the applicant has first obtained a certificate of convenience and necessity from its State telephone regulatory agency or (ii) in States that do not have an agency with authority to require the applicant to obtain a certificate of convenience and necessity, the Administrator, or the Governor of the Bank has first made a finding that use of the loan proceeds will not result in the duplication of facilities; and

(17) Revises the requirement that Telephone Bank borrowers must have the capability of producing net income or margins before interest at least equal to 150 percent of the interest requirements on all outstanding and proposed loans or such higher percentage as may be fixed by the Telephone Bank Board by permitting the Bank Board to lower as well as raise the percentage by requiring the ratio to be computed on a pretax instead of a posttax basis.

Committee Amendment

The Committee amendment strikes all after the enacting clause and inserts in lieu thereof an amendment in the nature of a substitute. In addition to several clerical and technical changes, the Committee amendment makes the following changes in S. 1300:

(1) Requires the prior approval of the President of the Federal Financing Bank before the Administrator of the Rural Elec-

trification Administration may repurchase certificates of beneficial ownership without penalty;

(2) Requires that the "standard" rate of interest that is charged on insured electrification and telephone loans be sufficient to produce anticipated interest income (including interest income from outstanding loans and any appropriated funds) that is equal to the total anticipated interest expense on all the outstanding obligations of the particular account;

(3) Requires that the Administrator make insured loans at the "special" rate of interest and provides that the borrower may satisfy the "financial hardship" portion of the "special" interest rate eligibility test if the borrower's in-service utility plant investment per consumer served is at least twice the national average of other borrowers in the same program;

(4) Requires that the Administrator establish a reserve in both the electrification and telephone accounts to cover the cost of loans made or extended at the "special" rate of interest and place annually in each reserve an amount equal to 1 percent of the preceding fiscal year's principal and interest payments made to the account. If the Administrator determines, as of the end of the fiscal year, that either reserve is inadequate to cover the projected 5-year costs of the "special" rate loans, he must so notify the Secretary of Agriculture, who must seek an appropriation to cover the deficiency. The amendment also requires that each loan made at the "special" interest rate be reviewed by the Administrator every 5 years and that the interest rate be adjusted to the then current "standard" rate if the borrower no longer qualifies for the "special" rate; and

(5) Requires that the Administrator, on the application of a cooperative located in a noncontiguous State not served by a statewide or multistate power grid, apply the same minimum financial standards separately to the distribution assets and the generation and transmission assets of such cooperative as are separately applied to cooperatives classified by the Administrator as being either a distribution or a generation and transmission cooperative.

Purpose and Need for Legislation

BACKGROUND

During the 53-year period from 1882, when the first central station electric generating system went into service, until 1935, only 10.9 percent of the farms in the United States received electricity.

Because of the high cost of providing electric service to rural areas, private utility companies were reluctant to undertake the challenge of providing service to such areas. It became apparent in 1935, however, that rural people would not get central station electric service at rates they could afford to pay without a helping hand from the Federal Government. Thus, the Rural Electrification Administration was created by Executive Order on May 11, 1935.

The REA was begun as part of a general program of unemployment relief under authority of the Emergency Relief Appropriation Act of 1935, with $100 million in funds made available for either loans or grants. Later that year, the President issued regulations which established REA solely as a lending agency, freeing it from many of the relief program restrictions and broadening the Administrator's authority to make decisions. Statutory provision for the agency was made in the Rural Electrification Act of 1936, and the REA became part of the United States Department of Agriculture in 1939.

Since its creation, the REA has helped bring light and power to practically every corner of rural America, raising the proportion of the farms receiving electricity to about 99 percent. REA borrowers also supply electricity to nonfarm rural establishments, including residences, businesses, schools, and churches, and they continue to meet the rising demand for power from all their consumers.

Loans made by REA were initially made at interest rates that fluctuated with the cost of money to the Government. In 1944, this rate was fixed by Congress at 2 percent, which was the approximate cost of money to the Government at the time. This rate of interest remained unchanged for nearly 30 years.

The lending authority under the Rural Electrification Act of 1936 was expanded in 1949 to include making loans for telephone service in rural areas. At that time, only 38 percent of this Nation's farms and ranches received telephone service. Today, the figure stands at 95 percent, a testimony to the effectiveness of this vital program.

As the capital needs of rural electric and telephone systems began to grow, it became evident that a supplemental source of financing was needed. In 1969, the National Rural Utilities Cooperative Finance Corporation (CFC) was formed by the rural electric cooperatives. Its loans to finance electric systems are obained from the private credit market. As of the end of 1982, CFC had provided more than $2.1 billion in long-term loans to its membership, which includes 826 systems.

To provide additional funding for telephone loans, the Rural Telephone Bank was established in 1971. The Bank has been provided with capitalization by the Federal Government in the form of stock purchases. The Bank makes loans available to eligible telephone borrowers to supplement the lending programs of the REA.

The benefits that the REA has brought to rural America are unquestioned. Today, millions of rural residents are able to enjoy the same standard of living as their city counterparts due in no small part to the programs administered by the agency. Farms, rural businesses, and small communities alike have grown and prospered because of our continued commitment to bring stable, affordable electric and telephone service to the people in these areas.

Rural Electrification and Telephone Revolving Fund

In May of 1973 (in Public Law 93-32), Congress amended the Rural Electrification Act of 1936 to establish the Rural Electrification and Telephone Revolving Fund and to make other modifications in the lending programs of the Rural Electrification Administration.

This revolving fund provides all the funds for REA direct lending to eligible rural electric and telephone borrowers. The original "seed capital" of the fund was provided by Congress and consisted of $7.4 billion in outstanding direct loans made by REA from 1953 through 1973, as well as other specified assets such as the cash REA had on hand representing funds provided by Congress but not yet advanced to borrowers. In 1976, another $455 million in notes was added to the fund, representing loan commitments made prior to establishment of the fund, but not advanced until after establishment of the fund. These obligations of REA borrowers comprised the assets of the fund and totaled $7.864 billion. REA continuously makes new loans from loan collections and, in this way, the assets are said to "revolve".

The funds used to make the loans that became the "seed capital" of the revolving fund were generally obtained through borrowings by REA from the United States Treasury. The notes of the Administrator to the Secretary of the Treasury which had been issued to obtain these funds were made liabilities of the revolving fund at the time the Act was amended in 1973.

Although the fund was made liable for the principal owed on these notes, all future interest payable on them was forgiven. These notes were written in various denominations and mature during the period 1993 through 2016.

The 1973 amendments to the Act provided authority to obtain additional funds for the revolving fund if its assets were not adequate to meet the annual loan levels set by Congress. The mechanism used to obtain these additional funds is the sale, by REA, of certificates of beneficial ownership to the Treasury. Generally, these CBO's are now sold to the Federal Financing Bank, an adjunct of the U.S. Treasury. These CBO's represent interests in pools of notes secured by mortages. Interest on CBO's is paid semiannually and the CBO's themselves are to be repurchased using assets of the revolving fund, after 30 years.

The first CBO, sold on March 31, 1976, was in the amount of $166,374,000 and carries an interest rate of 8.25 percent. The most recent CBO sale, on September 30, 1983, was for $155.8 million and carries an interest rate of 11.605 percent. Through September 30, 1983, total CBO sales have amounted to $3.5 billion.

Financial stress on the revolving fund that will, if unchecked, eventually result in the fund's insolvency has occurred as a result of the interrelationship between the lending levels of the REA program and the differential between the interest income to the revolving fund and the interest expense of the fund. The interest rates charged to REA borrowers (5 percent in most cases, and in unusual hardship cases, 2 percent) is insufficient to generate enough income to pay the fund's interest expenses on the money it borrows through the sale of CBO's. For example, the interest rate paid to the fund by REA borrowers averaged 4.90 percent in 1983, while the interest rate paid on CBO's sold to the Treasury averaged 10.85 during that same period.

As the demand for loan funds from the revolving fund grows, and if the differential between the revolving fund's lending and borrowing rates remains substantial, an increasing portion of the fund's resources will be needed to cover interest expense, and,

therefore, will not be available to fund loans. It is anticipated that, under law, the total annual interest expense of the fund will exceed total annual interest income beginning in the late 1980's. If unchanged, this negative interest differential will eventually erode all the fund's assets.

If the viability of the fund is to be maintained, it is clear that modifications are neccessary to correct the imbalance between its income and expenses. Prudent management of the revolving fund dictates that this issue be addressed in a timely manner so that further deterioration of the fund's assets will not occur. The bill contains several provisions to address this issue.

Waiving revolving fund repayments of certain Treasury loans

As mentioned previously, the 1973 amendment to the Rural Electrification Act of 1936 established the Rural Electrification and Telephone Revolving Fund with "seed capital" of approximately $7.9 billion. This amount represents the total outstanding indebtedness of borrowers to the Rural Electrification Administration. The repayment of principal and interest on these loans is made into the fund and is subsequently used to make new loans.

The funds used to make the initial loans were obtained by borrowing from the United States Treasury, and notes were issued by the Administrator of REA to the Secretary of the Treasury as evidence of this borrowing. The funds were then made available for lending to REA borrowers under sections 4, 5, and 201 of the Act. Each of these notes issued to the Secretary of the Treasury has a 40-year term and provides for a single payment at the end of that term. The first of these notes becomes due in 1993. In 1973, Congress stipulated that no interest would be paid to the Treasury on these notes. The value of this interest free loan to the revolving fund is estimated by REA to be over $25 million a month or over $300 million a year.

A key provision of the bill would relieve REA of the obligation to repay the $7.9 billion debt to the Treasury and make the notes representing that debt permanent equity capital of the revolving fund. This action would strengthen the financial position of the fund by reducing its obligations. It is anticipated that, if the revolving fund is required to repay this debt beginning in 1993, it would have to borrow similar amounts from the Treasury. The resulting interest expense associated with these new borrowings could have a very significant effect on the rural electric and telephone lending program.

The bill would permit the $7.9 billion to remain in the revolving fund, under Government control, for the future exclusive use of rural electric and telephone borrowers. This transfer will enable the revolving fund to support a level of lending consistent with anticipated demand as well as to ensure that interest rates charged to borrowers remain affordable. If at some future time the need for REA lending should cease, all assets and income of the fund would automatically revert to the Treasury.

Standard Interest rate

One of the most significant factors contributing to the difficulties confronting the revolving fund is the disparity between the rate of

interest charged to borrowers on loans made from the revolving fund and the rate of interest that the fund must pay on the money it borrows to make loans.

Current law mandates a fixed rate of interest of 5 percent on loans made from the revolving fund, except in unusual hardship cases in which a 2-percent rate may be charged. Recent borrowing by the fund, through the sale of certificates of beneficial ownership, has been at interest rates more than twice the 5 percent fixed rate charged to borrowers. This gap between the interest income and interest expense of the fund is substantial and is depleting the revolving fund. For example, during fiscal year 1982, there was an 8 percentage point difference in the rate the Rural Electrification Administration charged its borrowers (5 percent) and the average rate REA paid on its CBO sales (13 percent). This interest rate differential resulted in interest losses to the fund of about $40 million during fiscal year 1982, based on REA CBO sales of $528.4 million. During each of the past several years the revolving fund has taken in less in borrower repayments than it has disbursed in the form of loan advances and interest expense on CBO's. For example, total borrower loan repayments, including principal and interest, into the revolving fund were $815.1 million during fiscal year 1982, compared with loan disbursements of $1.05 billion and interest on CBO's of $308.3 million for the same period. For the period 1973 through 1982, total receipts of the revolving fund were $5.2 billion, compared with disbursements totaling $9.9 billion. As the revolving fund is required to raise more money to meet loan demand and borrows this money at interest rates significantly above the interest rate charged to REA borrowers, the cash flow difficulties of the fund will increase, and result in the sale of even more CBO's. Maintaining current loan program levels at the present statutory interest rates with a significant amount of borrowed money will result in the eventual bankruptcy of the fund.

The bill would relieve this financial stress on the revolving fund by eliminating the current 5 percent interest rate ceiling on electric and telephone loans and requiring the Administrator to establish standard interest rates for each program, not less than 5 percent, that will produce interest income to the fund (that is, the interest paid by REA borrowers) that, together with appropriations and interest income on existing loans, is equal to the total interest expense of the fund. Total interest expense includes interest payments made on all CBO's sold by the REA. This provision will help to ensure that the fund's cash flow position will remain in balance.

Thus, under the bill, REA borrowers will shoulder a larger portion of the cost of the revolving fund's borrowings. The standard interest rate will be adjusted periodically so that the expenses of the fund are appropriately reflected in the rates charged to borrowers. The Congressional Budget Office estimates that the amount of additional interest paid by borrowers to REA over the 1985–2010 period, assuming current lending levels (adjusted for inflation in future years) will be about $11.1 billion. Through this action, the fund will be able to sustain the additional borrowing that is necessary to maintain current loan program levels without a negative impact on the stability of the fund itself.

Special interest rate

The bill would mandate that electrification and telephone loans be made at an interest rate that is less than the standard rate for those borrowers who meet certain specified criteria.

This provision requires that an interest rate of not greater than one half the standard rate and not less than 2 percent be charged to borrowers that are experiencing hardship and meet specific criteria. The bill would expand the eligibility criteria for special rate loans to include such factors as consumer electric and telephone rates exceeding twice the national average of rates charged by other borrowers in the same program, average consumer density of 2 or fewer per mile, financial losses attributable to storm damage, natural disasters, or other occurances beyond the borrower's control, and the geographic service area having unusually low per capita income. The Committee believes that these factors should be taken into consideration in determining eligibility for special rate loans. Also, under the bill, the financial hardship portion of the eligibility criteria may be satisfied by showing that the borrower's investment in utility plant in service per consumer served is at least twice the national average of other borrowers in the same program.

The Administrator of the Rural Electrification Administration would be required to make loans at the special rate if he finds that a borrower meets the specified criteria and is experiencing financial hardship. The mandatory nature of this provision was determined to be necessary by the Committee to ensure that all borrowers who meet certain objective standards will be granted special rate loans. However, under the bill, the Administrator would still retain the discretion to determine whether the specified criteria have been met by the applicant.

Furthermore, the bill would require that a reserve be established consisting of 1 percent of all repayments to the electric and telephone accounts during the previous year to cover the cost of making loans at the special rate. If this reserve proves insufficient to cover the costs of all special rate loans, the Secretary of Agriculture is required to seek an appropriation to cover the deficiency.

The bill would effectively resolve the difficulties that have existed in administering the current discretionary special rate program. By establishing criteria that a borrower must meet for eligibility, it would ensure that those borrowers most in need of additional help will be able to receive it.

Ratios for supplemental financing

An integral part of the question of how best to provide for the long-term solvency of the revolving fund relates to the issue of supplemental financing.

The current Act provides that the Administrator of the Rural Electricfication Administration may require an applicant, who appears to be able to obtain a portion of its credit from a responsible coopoerative lender or other credit source at reasonable rates and terms, to apply for and accept a loan concurrently with an REA insured loan, subject to full use being made of the congressionally-authorized insured loan funds.

Under this authority, the Administrator has established a percentage of each electric applicant's credit needs that will be met from the revolving fund. In other words, the Administrator has established requirements for applicants to obtain supplemental financing in accordance with certain prescribed ratios. These ratios were established to provide for an equitable program relative to each borrower's ability to raise capital in the private credit market and to stretch the funds available from the revolving fund.

In the past, the Administrator has attempted to revise the regulations relating to these ratios to require more supplemental financing (thereby reducing the need for the fund to borrow high-cost capital through the sale of CBO's) for those distribution borrowers that have achieved a financial standard that would support greater non-REA financing. However, in appropriation Acts for fiscal years 1982 and 1983, Congress prescribed that the ratios for concurrent supplemental financing in effect as of July 15, 1982, be maintained. This prohibited the Administrator from implementing adjustments to the ratios.

The ratios in effect as of July 15, 1982, generally require that 30 percent of the applicant's credit needs be met from supplemental sources and the remaining 70 percent be met with 5 percent loans from the revolving fund. This requirement provides for the same level of financing from the revolving fund in the case of all nonspecial rate borrowers.

A provision in the bill would establish the 70–30 ratio as a permanent requirement in any year in which the program level for insured electrification loans is below $1 billion. The Committee believers that maintaining the current ratios when the program level is below $1 billion is necessary to ensure that REA loan applicants are treated uniformly and that use of the ratios do not reduce loan demand below the minimum lending levels prescribed by Congress.

Refinancing of loans

Another key provision of the bill that is designed to strenghten the revolving fund relates to the refinancing of certificates of beneficial ownership (CBO's). This provision will authorize the Administrator of the Rural Electrification Administration to repurchase, without penalty, outstanding CBO's when their interest rates are at least 1 percent above current rates. The provision is discretionary with the Administrator, and the authority to repurchase may only be exercised with the approval of the Federal Financing Bank.

A similar provision relating to loans guaranteed by REA would authorize the lender, upon the request of the borrower, to refinance these loans when the interest rate on the loan is at least 1 percent above current rates.

The provision relating to refinancing of CBO's would have the potential of lessening the financial burden on the revolving fund when interest rates decline and the fund could take advantage of the decreased rates. The decrease in interest rates through such refinancing would result in less interest expense to the revolving fund and, thus, less expense to be passed through to borrowers. The Committee believes that this action will strengthen the fund and help provide for its future solvency.

Provisions relating to REA telephone loan program

Several provisions in the bill specifically to the Rural Electrification Administration telephone loan program.

Current law prohobits loans being made for telephone service in areas other then a "rural area". The term "rural area" was defined in 1949 to mean any area of the United States not included within the boundaries of a community having a population greater than 1,500. The bill would revise this definition to increase this population limit to 2,500. The Committee believes this is a more realistic limit and will facilitate consolidations and equisitions that would improve the operating efficiencies of the systems involved.

The bill would also modify the definition of "telephone service" to specifically include the transmission of data and the transmission by wire, fiber, radio, light, or other visual or electromagnetic means. This provision would update the definition to reflect changes in the technology of telephone communications since the definition was last revised in 1962—22 years ago. Although this provison broadens the statutory definition of "telephone service" to reflect new technological developments, it still maintains the prohibition against ventures such as message telegram service, community antenna television service not intended exclusively for educational purposes, and radio broadcasting.

The current Act mandates the purchase of Class A stock in the Rural Telephone Bank by the Federal Government beginning in 1971 and ending in fiscal year 1991. Appropriations of $39 million annually are authorized for such purchases until the total amount of Class A bank stock purchased reaches $600 million. The bill would remove the requirement that this capitalization be completed by 1991. This will allow the total U.S. capitalization of the Rural Telephone Bank to reach the full $600 million when less than the maximum $30 million is appropriated for such stock purchase in any year or years up to 1991. The removal of this "sunset date" will allow Congress to provide for the purchase of additional stock of the Rural Telephone Bank in years beyond 1991, if necessary, in order to reach the $600 million goal.

The bill would eliminate the provision in current law which prohibits the Administrator of the REA from making telephone loans in any State not having a State regulatory body with authority to require an applicant to obtain a certificate of convenience and necessity unless the Administrator makes a finding that no duplication of facilities providing reasonably adequate service would result. A similar prohibition on loans made by the Telephone Bank would also be deleted.

These provisions in the bill do not preempt State jurisdiction or avoid the need for obtaining certificates of convenience and necessity from regulatory bodies where such certificates are required by the State. Elimination of these requirements would provide more flexibility to the REA and to the Telephone Bank and be consistent with the trend toward deregulation and greater competition in the telephone industry.

Some rural telephone systems have experienced difficulty because of the prohibition in current law which limits the ability of REA borrowers to make use of funds from the Rural Telephone

Bank to expand their area of service. Under this provision, Rural Telephone Bank loans to improve the efficiency, effectiveness, or financial stability of borrowers may not be used to finance the purchase of local exchange facilities if such facilities are greater in size than the borrower's at the time the borrower received its first loan from the Bank.

Since a borrower's first loan from the Telephone Bank may have been made more than a decade ago, this restriction has been an impediment to many telephone systems seeking to make acquisitions that could greatly enhance their viability and loan security. A provision in the bill would delete the size limitation on acquisitions of exchange facilities that can be financed by the Rural Telephone Bank for the above purposes.

Another provision in the bill relating specifically to telephone borrowers would change the Rural Telephone Bank's interest coverage test to provide for its computation before income taxes and to make it more flexible. To be eligible for a Rural Telephone Bank loan, a borrower must have the capability of producing net income or margins before interest equal to at least 150 percent of the interest requirements on all its outstanding and proposed loans, or such higher percent as may be fixed periodically by the Rural Telephone Bank Board. Generally accepted financial and industry practices require the net income or margins for this purpose to be computed before income taxes since tax liability varies from year to year. The bill would conform the REA method of calculating this ratio with the generally accepted practice.

Current law also allows the interest coverage requirement to be increased above, but not reduced below, the 150 percent level. Inability to reach this level has caused certain telephone borrowers to be ineligible for the higher rate loans made by the Rural Telephone Bank, and, therefore, they have had to wait for the availability of the revolving fund loans while the Rural Telephone Bank had funds available. The bill would give the Rural Telephone Bank Board the flexibility it needs to reduce, as well as increase, the 150 percent level when necessary to allocate available funds more equitably.

Subordination and accommodation of liens

Considerable difficulty has been experienced by some electric and telephone borrowers in attempting to obtain financing from non-Government sources for their capital needs. A provision in the bill seeks to resolve this difficulty by establishing criteria under which this financing may be obtained.

In order for lenders to be willing, in most cases, to make loans to borrowers, collateral must be pledged against the indebtedness. However, under current Rural Electrification Administration policy, REA maintains a lien on all property owned by an REA borrower, including all property acquired after the proceeds of the REA loan have been expended. This "after acquired" clause in the REA lien makes it exceedingly difficult for REA borrowers to obtain outside financing without an accommodation or subordination of these liens.

The problems which have occurred in resolving requests for subordinations or accommodations have resulted from the desire on

the part of the REA to have a "compensating benefit" for such action, such as reducing the term on existing notes or prepaying one or more of the notes. Also, questions are often raised relating to the protection of the Government's interest under such an arrangement.

The bill would provide that, as appropriate, the Administrator of REA must accommodate or subordinate the REA lien for the purposes provided in the Act and for purposes of refinancing. Further, the Administrator would also be required to accommodate or subordinate the REA liens, at the request of the borrower, for any purpose that would enhance the financial strength or revenue of the borrower or improve the efficiency, effectiveness or financial stability of the borrower, if the borrower has or will have the ability to repay its existing and proposed debts.

Under these provisions of the bill, the Committee intends that obtaining financing from another lender to enhance the financial strength or revenue of the borrower or improve the efficiency, effectiveness, or financial stability of the borrower is to be considered as a satisfactory compensating benefit for the Administrator's lien accommodation or lien subordination so long as the security for outstanding Government loans remains reasonably adequate. In determining whether the security is reasonably adequate, the Administrator shall take into consideration the projected revenues of the borrower in addition to the value of the facilities which secures the borrower's obligation to repay such loans.

This provision will help ensure that REA borrowers have adequate access to additional sources of non-Government credit, which in turn should enable them to obtain a greater share of their capital needs from these lenders.

Committee Consideration

HEARINGS

The Subcommittee on Agricultural Credit and Rural Electrification, chaired by Senator Paula Hawkins, held 3 days of hearings on S. 1300, the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1983. The hearings were held on March 20, April 12, and May 15, 1984.

During the hearings, testimony was received from 35 different witnesses including the Administration, organizations representing rural electric and telephone systems, the Congressional Budget Office, the General Accounting Office, several business associations, citizen groups, independent private consultants, and others interested in the rural electric and telephone programs. In addition, a number of statements were received for the records by individuals and organizations interested in S. 1300.

March 20, 1984

Senator Hawkins, Chairman of the Subcommittee on Agricultural Credit and Rural Electrification, opened the first day of hearings on March 20, 1984, by noting the success of the rural electrification program. She cited the increase in the percentage of farms which have been electrified from 12 percent in 1935 to 99 percent current-

ly, and the increase in the percentage of farms with telephone service from 36 percent when the REA telephone program began in 1949 to 95 percent today. She cited the establishment of the Rural Electrification and Telephone Revolving Fund in 1973, funded through the temporary assignment of $7.9 billion in outstanding loans due to be repaid to the U.S. Treasury beginning in 1993. She noted that the revolving fund's financial position has been eroding because income into the fund continues to be insufficient to cover the obligations of the fund.

Senator Huddleston, chief sponsor of S. 1300, said that congressional action is needed to keep the revolving fund self-sustaining and otherwise enable the rural electric and telephone systems to obtain adequate financing for their operations. He added that, without legislation to restructure the REA loan programs, in the near future there will be only two options—bail out the fund with tax dollars or greatly curtail the only source of financing for many rural electric and telephone systems.

According to Senator Huddleston, if the assistance provided through the REA revolving fund is curtailed, financing costs will escalate and put additional upward pressure on rural utility rates. On the average, consumers in rural areas already pay higher utility rates than city dwellers because of the high cost of providing service in areas of low population density.

The first panel of witnesses consisted of the Honorable Frank Naylor, Under Secretary for Small Community and Rural Development, and the Honorable Harold Hunter, Adminsitrator, Rural Electrification Administration (REA), U.S. Department of Agriculture. Mr. Naylor cited the value and commendable record of the REA in providing electricity and telecommunications to rural America and the Administration's continued support of these programs. He stated that S. 1300, however, was not the best method to resolve the fund's problems and could cost the American taxpayer, including rural electric and telephone subscribers, as much as $21 billion. He stated that if S. 1300 passed the Congress in its present form, the President would probably be advised to veto the legislation. He stated that the Committee should consider alternative proposals to S. 1300 in order to maintain the fund and protect the interests of the American taxpayer.

Mr. Hunter confirmed the Administration's desire to maintain strong rural electric and telephone programs now and in the future. He stated that S. 1300, as introduced, does not resolve the fund's problems, but merely delays, at great expense, the fund's insolvency. Under S. 1300, the fund's interest rates would remain relatively low for some time, but gradually increase to reach rates higher than the cost of Government borrowings. He stated that the simplest and most effective solution to the problem would be to gradually increase interest rates for borrowers in order to repay the fund's obligations, which could be accomplished despite keeping interest rates several percentage points below the Government's cost of borrowing. He stated that, for each percentage point increase the fund charges on new loans, the residential user, on average, would pay only an additional ½ cent per day, and would therefore pay only 60 cents per month if the interest rate charged on loans made from the fund is changed from the current 5 percent

to a 9 percent rate, a rate assumed sufficient to permanently solve the problems.

Mr. Larry Belluzzo, Program Analysis Staff Director for REA, presented the results of several comprehensive analyses of the proposals made to resolve the fund's problems. He stated that, even with the forgiveness of the $7.9 billion in loans to the Treasury, the revolving fund would still insolvent under most plausible scenarios, because the interest rates proposed in S. 1300 are simply insufficient to meet the fund's needs, and annual appropriations would be needed to continue the program.

The second panel consisted of Mr. Guy C. Lewis, President, Mr. Robert D. Partridge, Executive Vice President, and Mr. David A. Hamil, member, National Rural Electric Cooperative Association (NRECA), and Mr. Charles B. Gill of the National Rural Utilities Cooperation Finance Corporation (CFC). Mr. Lewis stated that the availability and cost of capital is of crucial importance to the future of the rural electrification program and that every effort must be made to continue current financing levels. He stated that the NRECA recognized the fund's problem and, therefore, sponsored a committe which made recommendations that, to a great extent, have been included in S. 1300. Long-term future considerations for rural electric borrowers and consumers can best be served by enactment of S. 1300, including the provisions that will increase the interest rates borrowers must pay.

Mr. Partridge stated that S. 1300 guarantees the continued stability and solvency of the fund and results in slightly higher rates for consumers—a price worth paying. He also stated that he believed the Administration's cost estimates of S. 1300 were based on faulty assumptions. He noted that under the $7.9 billion equity conversion called for in S. 1300, the Government would retain full control of the assets and that nothing in the proposed legislation would result in the "forgiveness" of any debt and that S. 1300 would reduce the need for future borrowings from the Treasury. Mr. Hamil stated that the NRECA study committee recommendations contained in S. 1300 are both reasonable and fair, and should be supported. He stated that S. 1300 would not slow the process of "weaning" rural electric borrowers from dependence on the REA. Reducing the role of the REA, however, cannot be accomplished overnight. The amount of subsidy being received by either investor-owned, municipal, or rural electric utilities is not important, but reasonable comparability of rates should be the determining factor in subsidy considerations of utilities. Mr. Gill stated that the CFC provides a source of long-term and short-term loans to supplement REA borrowings. CFC also provides loan guarantees for tax-exempt industrial development bonds. He said that REA is too rigid on granting accommodations which adversely affects the operating efficiency of rural electric systems. He noted that section 7 of S. 1300 would resolve the problem.

The third panel consisted of Mr. David C. Fullarton, Executive Vice President, National Telephone Cooperative Association, and Mr. Harold Peterson, Executive Director, National REA Telephone Association. Mr. Fullarton stated that most small, rural telephone systems are still unable to qualify for commercial financing and that REA policies deny borrowers access to outside financing. He

said that S. 1300 would resolve the problem and ensure continued financial health of the REA telephone program by helping the borrowers diversify their operations. Mr. Peterson stated that S. 1300 demonstrates that revolving fund borrowers are willing to assume a fair share of the responsibility for preserving the integrity of the fund. If rural telephone rates are to remain comparable with urban telephone rate, rural telephone companies must be free to offer new or enhanced services that, in competitive environment, may be duplicative of other facilities. S. 1300 improves the definition of telephone service without disturbing historical boundaries between telecommunications and CATV and broadcast radio.

April 12, 1984

Senator Hawkins opened the second day of hearings by noting that during the first hearing all witnesses agreed that action should be taken to ensure the financial soundness of the revolving fund, but that several witnesses differed as to the real effects of S. 1300 and its ability to achieve its stated purposes. She noted that many questions remained unanswered and that several studies have been completed on the REA program, the results of which would be shared during the hearing.

Senator Huddleston, in his statement, noted that during the previous hearing Mr. Frank Naylor repeatedly stated that S. 1300 will cost $21 billion. Senator Huddleston recalled that, in the previous hearing, he pointed out to Mr. Naylor that the Congressional Budget Office did not agree with that estimate, and Mr. Naylor responded that the Committee should review very carefully later determinations that both the Congressional Budget Office and the General Accounting Office made, indicating that they very strongly supported his position. Senator Huddleston noted that nowhere in the updated Congressional Budget Office or General Accounting Office analyses before the Committee is it stated that the cost of this legislation even approaches $21 billion.

Senator Max Baucus stated that S. 1300 ensures that rural electric and telephone systems will continue to provide high quality, affordable electric and telephone service to consumers. He testified that just because assets of the revolving fund become permanent capital does not mean that it is a "giveaway."

The first panel of witnesses consisted of the Honorable Thomas Healey, Assistant Secretary for Domestic Finance of the U.S. Department of the Treasury and the Honorable William A. Niskanen, Member of the Council of Economic Advisors. Mr. Healey stated that S. 1300 provides an unjustified forgiveness of $7.9 billion of debts owed to the U.S. Treasury and would be accomplished outside the budget and appropriations proccess, resulting in a method of "backdoor" financing. Further if the $7.9 billion is not repaid, the Government must make up the shortfall by either raising taxes or making additional borrowings by the U.S. Treasury. He expressed the concern that S. 1300 would establish a precedent that might later be cited with respect to repayment of the $135 billion in Federal borrowings currently financed through the Federal Financing Bank. Mr. Healey also testified that S. 1300 provides for the guarantee of loans to and/or subordination of liens with respect to tax-exempt entities, despite at least 24 statutes which preclude Federal

guarantees of the obligations of such tax-exempt groups. During questioning, Senator Zorinsky made reference to Mr. Healey's statement that the Administration believes REA programs should be funded only through appropriations. Senator Zorinsky noted that the Administration had recently requested a rescission of the first and only appropriations ever made for the REA revolving fund.

Mr. Niskanen stated that S. 1300 is an inefficient and inequitable method to assist rural residents. According to Mr. Niskanen the already large subsidy under the REA program distorts decisions made by electric power producers and by electric power consumers, producing an overinvestment in capital-intensive methods of energy production and consumption. The subsidy does not always go to those in need, but often to suburban or high income families which may already have low electric rates. Further, the consumers served by REA borrowers have changed significantly over time, as evidenced by the 50 percent increase in all REA subscribers since 1970, while the number of forms served increased only 0.3 percent. In addition, the characteristics of many cooperatives have changed significantly, and these changes should be considered in REA's lending policies.

Mr. Rudolph Penner, Director, Congressional Budget Office, stated that until 1944, interest rates charged to borrowers fluctuated with the cost of money to the Government. When the revolving fund was established in 1973, interest rates were established by law at 5 percent, slightly below the cost of money to the Government, which did not provide for the potential increase in the cost of money to the Government. The diferential between the interest rates charged to borrowers and the cost of obtaining funds is a primary factor contributing to the problem experienced by the fund today. Without a modification in the current program, beginning in 1990, or sooner if interest rates increase, the fund would need to stop making new loans to avoid insolvency resulting from borrowing at high rates and lending at low rates. Further, converting the $7.9 billion liability of the fund to equity would not, by itself, enable the fund to meet its obligations. However, in response to a written question, Mr. Penner stated that the cost of the legislation could be reduced and that a solvent revolving fund could result if S. 1300 was amended, as proposed by Senator Huddleston, to explicitly mandate that interest income must equal interest expense. He stated that the fund remains in a position to repay its obligations by raising its interest rates, but S. 1300 does not raise rates sufficiently and would lead to the necessity for another infusion of resources at a later date. Mr. Penner stated that the CBO cost analysis dicated that S. 1300 would increase the on and off budget Federal deficit by $10.4 billion. He also noted that under the current statutory 5 percent interest rate and current authorized loan levels, appropriations ranging between $10 billion and $17 billion would be necessary to cover the fund's losses. However, Mr. Penner further stated that if the increase in interest rates as proposed under S. 1300 were enacted, appropriations necessary to cover fund losses would be reduced to about $4 billion.

Mr. John Luke of the U.S. General Accounting Office stated that the S. 1300 interest rate formula does not produce enough revenue

for the fund to become self-sufficient and to retire the fund's debt with the Federal Financing Bank. However in response to a question from Senator Zorinsky, Mr. Luke stated that the revolving fund would be made solvent if S. 1300 were amended to explicitly mandate that interest income equal interest expense, as proposed by Senator Huddleston. However, Mr. Luke noted the position of GAO that an equally effective way of reducing subsidies would be to reduce the number of borrowers who receive subsidized loans from REA. He noted that loan subsidies in the case of REA cooperatives are 2.4 times greater than subsidies for investor-owned utilities. Mr. Luke testified that there is a subsidy of $2.35 per consumer in the case of IOU's and $41.04 per consumer for REA cooperatives. He stated that subsidies should be targeted to those cooperatives in need, such as those not financially sound or with unusally high consumer rates. More financing would then be available to cooperatives in need of such help and less financing would be available to those who could use the private credit market. Mr. Luke pointed out that GAO studies found that of 922 cooperatives, 386 could expect to obtain private financing at reasonable rates and terms. Out of 921 cooperatives, 199 had an equity ratio greater than the IOU average. and out of 921 cooperatives, 681 had electric rates lower than the average IOU residential rate and 280 had rates more than 21 percent lower than the IOU rates. Further, some cooperatives have expanded to generate power, provide financing, own and lease coal mines, procure fuel and fuel supplies and other private business services. Also S. 1300 continues the density criteria for hardship loans. Mr. Luke testified that this criteria is not an accurate indication of financial hardship because 61 percent of the 2-percent borrowers already have lower electric rates than neighboring IOU's. Mr. Luke stated that rate comparability should be an objective of REA's electric program.

The next panel consisted of Messrs. Rex Carpenter, General Manager, Nebraska Rural Electric Association; Lester Murphy, Jr., Executive Vice President, Kansas Electric Cooperatives, Inc.; and James M. Hubbard, Executive Vice President, North Carolina Association of Electric Cooperatives. Mr. Carpenter stated that S. 1300 is needed to balance the revolving fund in a timely manner and to ensure that the rural electrification loan program is able to continue in the future. He also stated that for most cooperatives which have service areas that are nonrural, their average number of consumers per mile is far below that of investor owned utilities. Mr. Murphy stated that without a strong rural electric program Kansas agriculture may not be able to withstand the projected impact of "rate shock", that is, the impact of electric and telephone rate increases. He noted that the high rates paid by some REA consumers in Kansas resulted from the cost of wholesale electric power. He also stated that natural disasters often inflict great damage on rural utility systems in Kansas and this is costly because Kansas electric cooperatives serve only 2.4 consumers per mile. Mr. Hubbard noted that cooperatives still, by and large, serve thinly populated areas and that rapidly growing areas have greater capital needs. He also stated that S. 1300 is the product of a year of intensive study by distinguished, experienced, and knowledgeable

leaders and that S. 1300 does not forgive any rural electric system debt.

The final panel for the second day's hearing consisted of Messrs. Robert R. Edmiston, Principal, Lehman Brothers Kuhn Loeb, Inc., and Lee Hogan, Director, Power and Communication Contractors Association. Mr. Edmiston pointed out that his company provides various investment banking services to rural electric cooperatives. He testified in support of S. 1300 and the lien accommodation and subordination provisions in particular. He stated that the provisions of S. 1300 would encourage the expansion of private market financing. If REA guarantees become insufficient to handle all requests, the private market could accommodate a portion but not all of the cooperatives' needs. He testified that a National Rural Utilities Cooperative Finance Corporation (CFC) study found, among other things, that the CFC is capable of enlarging its role in financing distribution cooperatives to the extent necessary and that individual G&T's have the capability of entering the market independently if they are credit-worthy. He also stated that subordination of the REA liens enhances credit-worthiness, yet fairness dictates that the Government's position should not be weakened by subordination. Mr. Hogan presented three choices to solve the problems of the revolving fund: abandon the REA program, dissolve the fund, or adopt S. 1300. He stated that S. 1300 provides for the continuation of a successful and efficient program at no cost to the Federal budget.

May 15, 1984

The third day of hearings was opened by Senator Hawkins who stated that, as a former Public Service Commissioner of Florida and former Member of the Rural Telephone Bank Board, she understoood the importance of providing rural electric and telephone service to rural Americans. She stated that she would do all in her power to ensure that rural Americans continue to receive these vital services. Reference was made to alternatives to S. 1300 which either have been introduced or proposed. She noted the continuing wide divergence of opinion as to the effect of S. 1300 and stated that one point was clear to her: whatever action is taken will have a multi-billion dollar impact on the Federal Treasury.

In his statement, Senator Huddleston expressed concern about some of the criticisms of S. 1300. He said that under S. 1300, the balancing of the REA revolving fund will be a joint effort with REA borrowers and the 25 million consumers served by REA-financed utilities.

The first witness, Anthony J. Gabriel, Deputy Inspector General, U.S. Department of Agriculture, testified concerning the audits of 110 electric distribution cooperatives conducted by the Office of Inspector General, as well as OIG's own analysis of S. 1300. He stated that the revolving fund's assets are diminishing, that interest rates should be increased, and that criteria for determining loan eligibility be changed.

Mr. Gabriel stated that the results of this audit indicated that a substantial number of cooperatives receiving REA loans have the financial capability to receive credit from the private market. Mr. Gabriel stated, however, that his criticism of the REA programs

was based on administrative and procedural deficiencies and not violations of law.

The first panel consisted of Dr. William Orzechowski, Director of Federal Budget Policy, Chamber of Commerce of the United States, and Mr. Baker A. Smith, Executive Vice President, U.S. Business and Industrial Council.

Dr. Orzechowski stated that the Chamber has frequently expressed its dissatisfaction with the lack of formal budget restraint on off-budget programs and has urged Congress to implement budget procedures to control them. He noted that the original mission of REA did not include a subsidy for borrowers, nor has past congressional action done so. It is the Chamber's position that an independent source of financing be provided for rural electric and telephone borrowers, with minimal Government assistance.

Mr. Smith stated the opposition of the U.S. Business and Industrial Council to S. 1300. He stated that the basis for this position was contained in a comprehensive 1984 USBIC study of various agricultural issues. The Council believes that the purposes of the original Act have now been achieved, since over 99 percent of our farms are electrified. Mr. Smith urged that Congress enact legislation to provide for a sound revolving fund by raising interest rates paid by REA borrowers and to encourage current borrowers to obtain credit from the private sector.

The next panel consisted of Dr. Joe D. Pace, Senior Vice President, National Economic Research Associates, Inc; Mr. Jack Doyle, Director, Agricultural Research, Environmental Policy Institute; and Ms. Jill Lancelot, Congressional Affairs Director, National Taxpayer's Union. Dr. Pace testified on the comparison of subsidies made to REA borrowers and those made to investor owned utilities (IOU's). He stated that his analysis showed that new 1983 subsidies to REA borrowers amounted to $40.89 per cooperative customer and $13.72 per IOU customer during each year of the life of those investments. Dr. Pace concluded that each year REA borrowers receive Federal subsidies far in excess of those provided to IOU's.

Mr. Doyle criticized the environmental record of REA cooperatives and noted that, through REA cooperated partnerships with investor owned utilities, public financing was being used for the private sector. He expressed concern over REA financing of nuclear power projects and over the competition between many power facilities and local farmers and ranchers for limited water supplies. Mr. Doyle concluded that the REA program should be made available to individual borrowers on the basis of need.

Ms. Lancelot stated the opposition of the National Taxpayers Union to S. 1300. It was the group's contention that the bill would not provide for revolving fund self-sufficiency. Furthermore, she stated that forgiveness of the $7.9 billion in debts owed to the Treasury would set a dangerous precedent for other off-budget programs. Ms. Lancelot stated that it is the contention of her organization that all existing indebtedness can be repaid by the fund without resulting in substantial rate increases to REA consumers.

The final panel consisted of Mr. John E. Horne, Executive Vice President, Florida Rural Electric Cooperative Association, and Mr. Angus Hastings, President, Clay Electric Cooperative in North Central Florida. Mr. Horne urged the passage of S. 1300 to stabilize the

revolving fund and to assure a continued source of loan funds for the rural segment of the utility industry. Mr. Horne noted that electric cooperatives in Florida, as in other States, serve a diverse population. He pointed out that 16 electric cooperatives in Florida serve 1.5 million people—10 percent of the State's population—living in an area accounting for two-thirds of the land mass.

Mr. Hastings discussed the increasing amounts of credit necessary to meet the needs of REA cooperatives to serve sparsely populated areas. He said that the annual interest expense per customer served by his cooperative went from $11.66 in 1973 to $43.90 in 1983 and that resulting rate increases are a burden on the many fixed income elderly served by the cooperative. Mr. Hastings noted S. 1300 is the result of input from many persons interested in a strong rural electric financing program and urged its expeditious passage.

COMMITTEE MARKUP

The Committee met on June 7, 1984, to consider legislation to amend the Rural Electrification Act of 1936. Two bills relating to rural electrification were introduced in the Senate and referred to the Committee. S. 1300, (introduced by Senator Huddleston and having 46 cosponsors), S. 2646 (introduced by Senator Simpson), H.R. 3050 (the House passed bill), and the Administration's legislative proposal were considered by the Committee.

Introductory statements were made by Chairman Helms and Senators Hawkins, Huddleston, Lugar, Melcher, Cochran, Pryor, Boschwitz, Boren, and Andrews. Under Secretary of Agriculture Frank Naylor expressed the Administration's views on the pending legislation. A representative of the Congressional Budget Office, Kathleen Gramp, gave a review of the Congressional Budget Office cost analysis of the bills.

The Committee adopted S. 1300 as the markup vehicle and proceeded to consider the various items in each bill.

Senator Boschwitz raised a concern about whether, in the best interest of enacting legislation to help rural electric and telephone borrowers this year, the Committee might first address the concerns raised by some non-Committee Senators before a bill was reported to the full Senate. Senator Huddleston responded that he believed it would be better to report out a bill and deal with any problems pertaining to floor action later.

After initial Committee consideration of the provision in S. 1300 to convert $7.9 billion of Rural Electrification Administration revolving fund liabilities to equity capital of the fund, Senator Lugar moved to strike this provision and maintain current law. The result of such action would be to maintain the requirement that the $7.9 billion in debts owed by the REA to the U.S. Treasury would be repaid beginning in 1993. By voice vote, the Committee defeated the motion and adopted the provision in S. 1300 pertaining to the conversion of the $7.9 billion of revolving fund liabilities to equity capital.

The Committee discussed the Administration proposal to pay the administrative cost of the REA programs from the revolving fund,

instead of through appropriations. The Committee agreed to maintain current law on this point.

The Committee discussed the provision in S. 1300 that would authorize the Administrator of REA to refinance certificates of beneficial ownership having a remaining term of at least 7 years when the CBO interest rate is at least 1 percent lower on new certificates. Senator Huddleston moved that S. 1300 be amended with the provision in H.R. 3050 requiring the President of the Federal Financing Bank to approve the repurchase of the certificates. Secretary Naylor was asked to comment on this provision. He stated that the Huddleston amendment would potentially eliminate the substantial cost exposure of such CBO refinancing, which could run as high as $15 billion or more over a 40-year period. The Committee adopted the Huddleston amendment on a voice vote.

The Committee next considered the provisions in the various bills relating to a change in the statutory interest rates charged on funds lent from the revolving fund. The provision in S. 1300 would amend current law—which sets this rate at 5 percent and, in special cases, 2 percent—to require the Administrator to establish and periodically adjust the "standard" interest rate so as to produce interest income equal to but not greater than the interest expense associated with the new borrowing of the fund. The provision in H.R. 3050 requires that the interest rate be sufficient to produce anticipated interest income that is equal to the total anticipated expense on all outstanding obligations of the fund. Under S. 2646, the interest rate would be determined by dividing the principal and interest expense by the interest income and then multiplying that quotient by the rate of interest charged on the most recently issued certificate of beneficial ownership. This rate would then be phased in over a 10-year period. The Administration proposal would set an interest rate that is not less than the current yield on similar Treasury securities adjusted to the nearest one-eighth of 1 percent, plus an allowance to cover administrative costs and probable insured loan losses.

After discussion of the various interest rate formulas among Senators and the Administration representatives, Senator Huddleston moved the adoption of the provision in S. 1300, as amended by the provisions in H.R. 3050. He stated that the language in H.R. 3050 would help achieve the objective of providing a stable and self-sustaining revolving fund. Senator Lugar moved the adoption of a substitute amendment—the interest rate provision in S. 2646. Senator Lugar described the substitute as a compromise between the formula found in S. 1300 and the Administration bill. He advocated that the Committee resolve the problems of the revolving fund permanently and, to accomplish that, the interest rate charged to borrowers must be sufficient to make the fund solvent. He pointed out that the issue is not whether the Committee eliminates the REA program, but rather whether the Committee provides for program stability in perpetuity. This can be achieved by establishing a borrower's interest rate that ensures equality between the rates charged on money coming into the fund and that charged on money being lent from the fund. Senator Lugar stated that an interest subsidy is still maintained under S. 2646.

The representative of the Congressional Budget Office, Ms. Gramp, was asked to provide an analysis of the interest rate formulas in the bills. She noted that the difficulty in projecting the effect of the language found in H.R. 3050 was in determining how the language is to be interpreted. She stated that there are at least three different ways to implement this language. Ms. Gramp said that, under the interpretation providing the highest interest rates, the fund could remain solvent through the year 2010, the last year projected by the Congressional Budget Office. She further explained that, under S. 2646, the interest rates would be relatively stable at approximately 9 percent and that under S. 1300, the interest rates would eventually go to market rates.

Chairman Helms read a letter from Senator Gorton requesting that the Congressional Budget Office provide a comparison of the interest rates to cooperative borrowers under the various bills, and asking under which formula borrowers would pay the lowest rates in the long term. Ms. Gramp responded that the Congressional Budget Office analysis showed that, between 1984 and 2010, interest rates under S. 1300, with or without the interest rate formula added in H.R. 3050, would average about 1 percent lower than under S. 2646. She explained further that the Congressional Budget Office analysis showed that toward 2010 and beyond, it appears that the interest rate under S. 1300 will increase as interest expense to the fund increases and will approach and exceed the Treasury rate. Additionally, Ms. Gramp stated that, under the formula in S. 2646, the interest rate should begin to decrease by the year 2010.

By voice vote, the Committee rejected the Lugar substitute amendment and adopted the Huddleston amendment to include the interest rate formula found in S. 1300, as amended by the provision in H.R. 3050.

During discussion of the "special" rate loans, Senator Zorinsky offered an amendment to make it mandatory for the Administrator of the REA to make insured loans at the "special" rate if the applicant meets certain specified criteria. The amendment would also permit an applicant to meet the amendment's hardship test if its in-service utility plant investment per consumer served is at least twice the national average of other borrowers in the same program. The amendment further provided that 1 percent of the yearly repayments to the revolving fund would be set aside in a reserve to cover the cost of special rate loans. The amendment also require that the special rate loans be reviewed every 5 years to determine if the borrower still meets the eligibility criteria associated with these loans. Senator Zorinsky explained that his amendment would more tightly restrict the number of cooperatives that could qualify for special rate loans. The number currently qualified to receive these loans is approximately 110; Senator Zorinsky stated that the number eligible for such loans under his amendment would be reduced to 60.

Secretary Naylor expressed concern over the mandatory provisions which, he said, would limit the discretion of the Adminsitrator to apply sound business criteria to the special rate loan program. Senator Huddleston pointed out that, under the Zorinsky amendment, the cooperative paying the standard rate would in fact

provide a subsidy for the special rate loans. The Committee adopted the Zorinsky amendment on a voice vote.

The Committee discussed the provision in S. 1300 that would make mandatory the guaranteeing of certain loans made by the Rural Telephone Bank, the National Rural Utilities Cooperation, or other legally organized lending agencies. This provision also broadens the definition of guaranteed loans to include refinancing. The Administrator would also be required to subordinate or accommodate liens or mortgages in certain instances. Chairman Helms inquired as to the need for mandatory loan guarantee authority. Senator Huddleston responded that the language was necessary to ensure that all appropriate applications were approved. Secretary Naylor stated that the Administration believes that discretion is necessary to ensure that the best interests of all parties are served under such guarantees. He further noted that requiring subordination or accommodation in certain instances could jeopardize the Government's security. Also, certain activities that may be financed through subordination or accommodation should be reviewed by the Administrator to determine if they would be in the best interests of the cooperative's members of the Government.

Senator Huddleston explained that the guarantee provision in section 7 of S. 1300 is not intended to require that the REA Administrator actually guarantee any specific loan, but rather would require only that a program and the procedures be established for such guarantees. He further explained that the intent of this provision is for the REA Administrator to maintain fully authority to decide whether or not a particular borrower is qualified for a loan guarantee. With respect to the accommodation and subordination provisions of S. 1300, Senator Huddleston maintained that the Government's interests are adequately protected under those provisions.

The Chairman inquired as to the provision in H.R. 3050 regarding subordination or accommodation. He noted that H.R. 3050 requires that the Administrator find that the Government's security will not be jeopardized before an accommodation or subordination would be granted. Senator Huddleston explained that because provisions in S. 1300 required a finding that the loan will be repaid, the Government's interests are adequately protected. He stated that the Committee's intent is not to force the Administrator into making a "bad" loan.

Senator Zorinsky offered report language to clarify the intent of the loan guarantee, lien accommodation, and subordination section. The report language was agreed to along with this section of S. 1300.

The Committee next discussed section 8 of S. 1300 regarding the amount of supplemental financing that will be required of REA borrowers. Mr. Hunter, in responding to a question, noted that from the establishment of the revolving fund in 1973 until recently, the Administrator had discretion to establish the portion of each new borrower's loan needs that could be met from the revolving fund. Mr. Hunter further stated that, 2 years ago, Congress directed that the ratios then in effect (generally 70 percent from the revolving fund and 30 percent from supplemental sources) be maintained. Mr. Hunter related the concern of the Aministration that

flexibility is needed to establish equitable ratios so that interest subsidies can be targeted on the basis of need, rather than under the current "blanket" arrangement.

Senator Huddleston noted that he could see some value in flexibility in establishing the ratios and that, if this provision causes particular difficulty, it could be addressed at a later time. The Committee adopted the language in section 8 of S. 1300 by voice vote.

The Committee discussed the Administration proposal that would put the REA program on budget. Current law requires that REA borrowing and lending activity remain off-budget. The Committee, by voice vote, agreed to retain current law.

The Committee discussed section 9 of S. 1300 permitting purchases by the United States of stock of the Rural Telephone Bank beyond fiscal year 1991. The provision was agreed to by voice vote.

Senator Cochran, on behalf of Senator Stevens, asked the Committee to consider an amendment pertaining to a cooperative in Alaska. This amendment would require the Administrator to apply the same minimum financial standards (Times Interest Earned Ratio) separately to the distribution assets and to the generation and transmission assets of a cooperative borrower located in a noncontiguous State not served by a statewide or multistate power grid as are applied separately to cooperatives classified as being either a distribution or a generation and transmission cooperative.

There was some discussion as to whether this situation exists with other cooperatives and whether the adoption of the amendment would involve more than the one cooperative in Alaska. Mr. Hunter assured the Committee that, to the best of his knowledge, the unique circumstances involved with this issue pertained solely to the Chugach Electric Association in Anchorage, Alaska.

The Committee adopted Senator Cochran's amendment by voice vote.

The Committee understands that Chugach Electric Association, a REA cooperative and the State of Alaska's largest electric utility in terms of both distribution and generation and transmission, faces a set of unique problems which merit and require the assistance of the Administrator. In its capacity as banker of Chugach, REA has in the past used its powers—or failed to use its full legal authority—in a manner that interferes with planning and frustrates long-range objectives to secure non-Federal sources of financing on reasonable terms and conditions. The Committee is concerned about this matter and feels that this cooperative, which is in transition and which is reviewing alternative financing and organizational options, should receive the full assistance and coooperation of REA. The Committee, therefore, fully expects that in the future the REA will utilize its existing legal authority to: (1) permit Chugach to increase member-owned equity in its electrical utility system; (2) assist Chugach in obtaining financing, capital and credit from other sources in addition to REA; (3) provide Chugach advice and assistance, when required, in planning and developing regional power supply and transmission facilities and systems in which cooperatives, municipal power systems, and State or Federal entities can appropriately participate; and (4) facilitate for Chugach merg-

ers, consolidations, acquisitions or other changes in forms of organization and financing relationships in a flexible manner.

The Committee then agreed to report S. 1300, as amended, by voice vote.

Section-by-Section Analysis

Section 1

Section 1 provides that the bill may be cited as the "Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984".

Section 2

Section 2 of the bill amends section 201 of the Rural Electrification Act of 1936 (the "Act") by repealing the requirement that a telephone borrower obtain a State regulatory agency certificate of convenience and necessity as a condition of eligibility for obtaining a loan under section 201 of the Act. Repeal of this provision would not preempt any requirement imposed on a utility by a State for a certificate of convenience and necessity or otherwise restrict State telephone regulatory authority generally. Section 2 also repeals the requirement that the Administrator make a determination that a telephone borrower will not use the proceeds of a loan to duplicate existing telephone facilities providing reasonably adequate service in States that do not have a telephone regulatory agency empowered to issue certificates of convenience and necessity.

A similar amendment is made to section 408 of the Act by section 10(3) of the bill. Section 408 governs loans made to telephone cooperatives by the Rural Telephone Bank.

Section 3

Section 3 of the bill amends the definitions in section 203 of the Act. The definition of the term "telephone service" is amended to specifically include communication service for the transmission of "data". The means of transmitting information included within the definition is also revised to specifically include wire, fiber, radio, light, or other visual or electromagnetic means.

Section 3 of the bill also amends the definition of the term "rural area", for purposes of the telephone program, by expanding it to include any area of the United States not included within any incorporated or unincorporated city, village, or borough having a population in excess of 2,500. Under current law, the population figure is set at 1,500.

Section 4

Section 4 of the bill amends section 302 of the Act. Section 4(1) amends the section heading to add the term "equity" to the heading. Section 4(2) amends section 302(a) to provide that all long-term notes previously issued by the Administrator of the Rural Electrification Administration to the Secretary of the Treasury to obtain funds for loans made under sections 4, 5, and 201 of the Act shall become equity capital of the Rural Electrification and Telephone Revolving Fund. Under current law, these long-term notes are liabilities of the revolving fund.

Section 4(3) amends section 302(b)(2) of the Act (i) to conform this section to section 302(a) of the Act, as amended, (which makes certain REA notes equity instead of debt), (ii) to delete the limitation that payments, from the assets of the fund, of principal and interest on loans to the Administrator be made "when due", and (iii) to specifically authorize the use of assets of the revolving fund to pay principal and interest on certificates of beneficial ownership issued to the Secretary of the Treasury or in the private market.

Section 4(4) adds a new subsection (c) to section 302 which requires the Administrator to establish two separate accounts within the revolving fund. These accounts are to be identified as the Electrification Account and the Telephone Account. All assets, liabilities, income, expenses, and equity in the revolving fund that are attributable to the operations of the electric loan program will be accounted for in the Electrification Account. The assets accounted for in the Electrification Account shall be used exclusively in the electric loan program for the purposes specified for the revolving fund. All similar assets, liabilities, income, expenses, and equity in the revolving fund that are attributable to the telephone loan program will be accounted for in the Telephone Account. The assets accounted for in the Telephone Account shall be used exclusively in the telephone loan program for the purposes specified for the revolving fund.

Section 5

Section 5 of the bill amends section 304 of the Act to authorize the Administrator, after having obtained the prior approval of the President of the Federal Financing Bank, to repurchase any certificate of beneficial ownership whenever (i) the interest rate on the certificate exceeds the interest rate to be paid on similar new certificates by 100 basis points (1 percent) or more, and (ii) the remaining term of the certificate is 7 or more years. Any such repurchase will be made without penalty.

Section 6

Section 6 of the bill amends section 305 of the Act. Section 6(1) revises section 305(b) of the Act to provide that the Administrator shall establish and periodically adjust a "standard" rate of interest for each account for insured loans under regulations promulgated within 120 days of the effective date of the bill. The "standard" rate of interest may not be less than the current statutory rate of 5 percent. The Administrator is to set the "standard" rate of interest for loans made from each account during a specified period of time such that the interest income produced from the loans (exclusive of loans made at the "special" rate of interest) will equal, but not be greater than, the anticipated interest expense on the account's obligations required to be issued or sold during the period to cover loan advances and interest expenses. The amount of the obligations to be issued or sold for each account will be determined by deducting (i) the sum of all principal and interest receipts and any funds appropriated to replenish the revolving fund for losses on loans made at the "special" rate of interest from (ii) the sum of the loan advances and interest expenses incurred in the account during the period. In all cases, however, the "standard" rate of interest, and

any subsequent adjustment to it, shall be set so as to be sufficient to produce total anticipated interest income from each account (including any appropriated funds and interest income from outstanding loans) that will equal total anticipated interest expenses on all outstanding obligations of the account. The "standard" rate shall be established or changed after taking into consideration the objectives of the Act. The "standard" rate established under the bill and any adjustment to it shall only apply to loans made after the effective date of the establishment or change.

Revised section 305(b) of the Act, as amended by section 6(1) of the bill, also provides that the Administrator shall make insured loans at a "special rate of interest, not lower than 2 percent nor more than one-half the "standard" interest rate, if the Administrator finds, under guidelines established within 120 days after the effective date of the bill, tht the borrower:

(1)(a) charges rates exceeding twice the national average of rates charged by other borrowers in the same program, or cannot provide service consistent with the objectives of the Act without charging rates so high as to create a substantial disparity between those rates and the rates charged for similar service by other suppliers in the same or nearby areas;

(b) has an average consumer density of two or fewer per mile of line;

(c) has experienced financial losses due to storm damage, natural disasters, or other occurrences beyond its control; or

(d) serves geographic areas having unusually low per capita income; and

(2) is experiencing financial hardship, as determined by investment in utility plant in service per consumer served being at least twice the national average of other borrowers in the same program, or other financial or other hardship, through extenuating circumstances, as determined by the Administrator.

The regulations promulgated under revised section 304(b) of the Act shall not take effect until (i) the regulations have been transmitted to the House Committee on Agriculture and the Senate Committee on Agriculture, Nutrition, and Forestry and (ii) 30 calendary days of continuous session of Congress have expired after the date of transmittal.

Section 6(2) redesignates existing subsection (c) of section 305 as subsection (d) and deletes the requirement that the Administrator sell or insure, without undue delay, the loans that have been made to borrowers.

Section 6(3) adds a new subsection (c) to section 305. The new subsection provides that the Administrator shall establish a reserve in both the electrification and telephone accounts to cover the cost of loans made at the "special" rate of interest. At the beginning of each fiscal year, the Administrator shall place in the reserve in each account an amount equal to 1 percent of the account's principal and interest receipts received during the preceding fiscal year. The Administrator must estimate the total cost for a 5-year period of al "special" rate loans made or extended during the fiscal year and apply the reserve funds in each account against these estimated costs. If the Administrator determines that, as of

the end of the fiscal year, either reserve is inadequate to cover the estimated cost, the Administrator must promptly notify the Secretary of Agriculture, who shall include in the Secretary's next supplemental budget estimate or request sumbitted to the President or the Office of Management and Budget, a request for funds to cover the estimated deficiency. The Secretary shall concurrently, with the submission of the request for appropriations to the President or the Office of Management and Budget, submit this request to the House Committee on Appropriations, the House Committee on Agriculture, the Senate Committee on Appropriations, and the Senate Committee on Agriculture, Nutrition, and Forestry.

The new subsection also provides that the Administrator must review each loan made at the "special" interest rate every 5 years to determine whether the borrower continues to qualify for the "special" rate loan. The Administrator shall (i) extend the loan for an additional 5-year period if the borrower continues to qualify or (ii) adjust the interest rate upward to the then current "standard" rate if the borrower no longer qualifies for the "special" rate.

Section 7

Section 7 of the bill amends section 306 of the Act. Section 7(1) designates the current text of section 306 as subsection (a).

Section 7(2) amends subsection (a), as redesignated by section 7(1), to provide that, in order to encourage and assist electric and telephone borrowers to develop and achieve the financial strength necessary to satisfy their credit needs from other sources and to improve their financial stability, the Administrator is required (rather than authorized, as is now the case under current law) to provide financial assistance to borrowers for the purposes provided in the Act and for purposes of providing refinancing. The financial assistance will consist of guaranteeing the full amount of loans made by the Rural Telephone Bank, the National Rural Utilities Cooperative Finance Corporation, and any other legally organized lending agency or lender approved by the Administrator, or by accommodating or subordinating liens or mortgages held by the Administrator, or by any combination of such guarantee, accommodation, or subordination. Current law does not authorize guarantees to be made to a lender that is not a legally organized lending agency.

The Administrator is also required to accommodate or subordinate liens or mortgage at the request of the borrower, notwithstanding any other provision of the Act, for any purpose that would enhance the financial strengths or revenue of the borrower or improve the efficiency, effectiveness, or financial stability of the borrower, upon a finding that the borrower has, or will have, the ability to repay its existing and proposed indebtedness.

Section 7(3) amends section 306 by expanding the definition of the term "guaranteed loan" to include loans that have been refinanced by any eligible lender and loans that have been made or refinanced by a lender approved by the Administrator.

Section 7(4) adds two new subsections to section 306. New subsection (b) requires the Administrator to promulgate rules and regulations within 90 days of the date of enactment of the bill for the guarantee of loans and the accommodation and subordination of

liens or mortgages. These rules and regulations shall not take effect until (i) they have been transmitted to the House Committee on Agriculture and the Senate Committee on Agriculture, Nutrition, and Forestry and (ii) 30 calendar days of continuous session of Congress have expired after the date of transmittal.

New subsection (c) authorizes the lender of a loan guaranteed by the Administrator, upon the request of the borrower and without penalty to the borrower, to lower the interest rate charged on any advance made under the guranteed loan to the rate charged for similar new advances then being made or purchased by the lender. The lender is authorized to take this action whenever (i) the interest rate on the advance made under the guaranteed loan is 100 basis points (1 percent) or more higher than the rate of interest charged for similar new advances being made or purchased and (ii) the guaranteed loan has a remaining term of 7 or more years. No interest rate adjustment on such an advance may be made at intervals of less than 7 years.

Section 8

Section 8 amends section 307 of the Act to provide that whenever the minimum loan level established by law for rural electrification insured loans is less than $1 billion in any fiscal year, rural electrification borrowers shall obtain concurrent supplemental financing from other credit sources in accordance with the criteria and ratios that were in effect as of July 15, 1982.

Section 9

Section 9 amends section 406(a) of the Act by repealing the provision ending, in 1991, the obligation of the United States to furnish capital to the Rural Telephone Bank. The effect of this provision is to remove the limit on the time period in which the United States is to provide $600 million in capital to the Rural Telephone Bank.

Section 10

Section 10 amends section 408 of the Act. Section 10(1) amends section 408(a) by deleting the provisions in current law that (i) require the approval of the Secretary of Agriculture for the acquisition of any telephone lines, facilities, or systems financed by Rural Telephone Bank funds made available under section 408(a)(2), (ii) require that the location and character of any facilities acquired with Rural Telephone Bank loan funds made available under section 408(a)(2) be such as to improve the efficiency, effectiveness, or financial stability of the borrower's telephone system, and (iii) limit the size of any acquisition of exchange facilities for local telephone service acquired with Rural Telephone Bank loan funds made available under section 408(a)(2) to the size of the borrower's system at the time it received its first loan from the Rural Telephone Bank, taking into account the number of subscribers served by the borrower, the borrower's miles of line, and the plant investment of the borrower.

Section 10(2) amends section 408(b)(4) by revising the current Rural Telephone Bank loan eligibility requirement that a telephone borrower have the capability of producing net income or margins before interest equal to at least 150 percent of the interest

requirements on all outstanding and proposed loans or such higher percent as may be fixed by the Rural Telephone Bank Board. The amendment would (i) permit the bank board to fix a different (higher or lower) percentage than the current 150 percent in order to allocate available funds equitably among borrowers or to improve the marketability of the telephone debentures and (ii) require that the borrower's financial capability be measured against such percentage on a pretax, instead of a posttax, basis.

Section 10(3) deletes paragraph (5) of section 408(b). Paragraph (5) currently prohibits the Rural Telephone Bank from making a loan to any applicant that is subject to a State telephone regulatory body unless the applicant has first obtained a certificate of convenience and necessity from the State regulatory body. Repeal of this provision would not preempt any requirement imposed on a utility by a State for a certificate of convenience and necessity or otherwise restrict State telephone regulatory authority generally. Paragraph 5 also prohibits the Rural Telephone Bank from making loans to any applicant located in a State that does not have a telephone regulatory agency empowered to issue certificates of convenience and necessity, unless the Governor of the Rural Telephone Bank determines that the loan proceeds will not be used to duplicate existing lines, facilities, or systems that provide reasonably adequate service.

A similar amendment is made to section 201 of the Act by section 2 of the bill. Section 201 governs loans made to applicants by the Administrator.

Section 10(3) also redesignates paragraph (6) of subsection (b) as paragraph (5) and revises the definitions contained therein to conform the definitions to the deletion of current paragraph (5).

Section 10(4) redesignates paragraph (7) of subsection (b) as paragraph (6).

Section 11

Section 11 amends section 410 of the Act by deleting subsection (b) and redesignating existing subsection (c) as new subsection (b). Subsection (b) of current law provides that, when all the class A stock of the Rural Telephone Bank that is owned by the Government has been retired, Rural Telephone Bank loans shall no longer be subject to the restrictions on the acquisition of telephone lines, facilities, or systems that are currently prescribed in the provisos to section 408(a)(2) of the Act. This deletion is a conforming change resulting from the amendment that eliminates the restrictions in section 408(a).

Section 12

Section 12 adds a new section 17 at the end of title I of the Act. The new section provides that the Administrator shall, upon the application of a cooperative borrower located in a noncontiguous State not served by a statewide or multistate power grid, apply the same minimum financial standards, such as the "Times Interest Earned Ratio", separately to the distribution assets and to the generation and transmission assets of the cooperative as are separately applied to cooperatives classified by the Administrator as being

either a distribution cooperative or a generation and transmission cooperative.

Section 13

Section 13 provides that the bill shall become effective upon the date of enactment, except that the Administrator shall continue to make insured loans to electric and telephone borrowers at the interest rates provided under section 305(b) of existing law (5 percent and not less than 2 percent, respectively) until the regulations setting the new interest rates, as provided in new section 305(b), are effective.

Administration Views

On June 6 and June 7, 1984, Chairman Helms received letters from Richard E. Lyng, Acting Secretary of Agriculture, R. T. McNamar, Acting Secretary of the Treasury, and David A. Stockman, Director, Office of Management and Budget, expressing the Administration's strong opposition to the enactment of S. 1300. The three letters follow:

Department of Agriculture,
Office of the Secretary,
Washington, DC, June 6, 1984.

Hon. Jesse Helms,
Chairman, Committee on Agriculture, Nutrition, and Forestry, U.S. Senate, Washington, DC.

Dear Mr. Chairman: I want to take this opportunity to again state this Department's views on S. 1300. The Department is strongly opposed to S. 1300 because it provides a substantial increase in subsidies which are not warranted to the electric and telephone cooperatives. The rural electric cooperatives have benefited from a wide range of subsidies, including the subsidized direct loans and 100 percent loan guarantees currently provided by the Rural Electrification Administration, an agency of the Department of Agriculture. However, it is my view that no appropriate justification has been provided for the substantial increase in subsidies and U.S. Government risks which are incorporated in this bill. It is my view that no further subsidies are warranted as represented by the proposals incorporated in S. 1300. I, therefore, strongly urge the Committee to reject this legislative proposal.

Should S. 1300 and its companion legislation, H.R. 3050, pass in essentially its current form, I would be left with no choice but to strongly recommend to the President that he withhold his approval of such a bill. As we have previously discussed, it is the Administration's belief that a strong, healthy rural electric program remains important to insuring the economic health and quality of life of rural areas.

The Departrment looks forward to working with the Congress to find appropriate means of effectively dealing with the revolving

fund problem related to the Rural Electrification Administration over the next few years.

Sincerely,

RICHARD E. LYNG,
Acting Secretary.

THE SECRETARY OF THE TREASURY,
Washington DC, June 6, 1984.

Hon. JESSE HELMS,
Chairman, Committee on Agriculture, Nutrition and Forestry, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: I am writing to clarify the Department's views on S. 1300, the "Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1983," which is scheduled for action by your Committee on June 7. The Department strongly opposes enactment of S. 1300.

It would add to the billions of Federal dollars already granted under existing subsidy programs to rural electric cooperatives. The further large increases proposed under S. 1300 are not justified.

The rural electric cooperatives have benefited historically from a wide range of subsidies, including subsidized direct loans and 100 percent loan guarantees, retention of essentially tax-exempt status while taking advantage of tax incentives (e.g., safe harbor leasing) available to fully taxable entities, tax-exempt municipal bonds for pollution control equipment, and preferential access to low-cost Federal power. No justification for the large increases in subsidies and in U.S. Government risk proposed by the bill has, however, been provided. Thus no further subsidies are warranted. We, therefore, strongly urge the Committee to reject this legislation.

Were the proposed legislation to pass the Congress in essentially its current form, I will not hesitate to recommend that the President withhold his approval of such a bill.

The Office of Management and Budget has advised that there is no objection to the submission of this report to your Committee and that enactment of S. 1300 in its present form would not be in accord with the President's program.

Sincerely,

R.T. MCNAMAR,
Acting Secretary.

EXECUTIVE OFFICE OF THE PRESIDENT,
OFFICE OF MANAGEMENT AND BUDGET,
Washington, DC, June 7, 1984.

Hon. JESSE HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: I am writing to clarify the Administration's views on S. 1300. The Administration is strongly opposed to S. 1300 because it provides a substantial increase in subsidies to the already heavily subsidized electric and telephone cooperatives. The Federal taxpayer dollars going to rural electric cooperatives

over the last 10 years have resulted in estimated (on and off budget) spending of $31.8 billion. The economic value of the subidies and benefits is estimated at over $38 billion.

Two independent studies, by the Congressional Research Service and by National Economic Research Associates, Inc., support the conclusion that total Federal subsidies to REA borrowers are greater than any Federal subsidies provided to private utilities on a per customer basis. The 1982 NERA study conservatively estimates that for a new utility investment made in 1981, taking into account tax changes under ERTA and TEFRA, the annual subsidy per customer is more than three times greater for co-ops than for private utilities.

In addition to the above benefits, REA administrative costs to assist these borrowers totaled about $200 million over the last decade; nearly all cooperatives' revenues were exempt from Federal income taxes; and cooperatives had preferential access over private utilities to low-cost Federal power.

Not surprisingly, electric rates charged by REA borrowers on average are lower than the rates charged by other electric utilities.

—Nationwide, REA borrower electric rates are about 12 percent lower than rates charged by other utilities.

—Even on an individual neighbor-to-neighbor comparison, rates charged by REA electic borrowers to residential customers are-*significantly lower* than rates charged by neighboring non-REA utilities in 80 percent of the States with REA assistance.

In an independent report to Congress, the U.S. Comptroller General (GAO) concluded that residential customers served by REA borrowers pay *less* for the same amount of electricity used by residential customers of private utilities. The 8.5 million residential customers served by cooperatives receive lower cost power on average than the 63.8 million residential customers served by investor-owned utilities.

The original purpose of the agency and 1936 Act was to bring electric and telephone service to farms and rural areas. About 99 percent of farms and rural areas are electrified and about 95 percent have telephone service.

Furthermore, telephone program borrowers have already received substantial tax benefits under the reforms enacted in 1981 (ERTA) and 1982 (TEFRA), and the existing REA subsidy programs, including 5% direct REA loans, subsidized RTB loans, and the FFB direct loans (REA loan guarantees). Many of the telephone companies either have the capability or already borrow in private credit markets. In view of the preceding, increases in Federal subsidies as contained in the bill are not justified and would only increase reliance on Treasury lending.

S. 1300 would increase the Federal deficit by at least $19 billion over the next several years by:

—forgiveness of $7.9 billion in loan principal due Treasury beginning in 1993.

—refinancing of CBO's (borrowings from the Treasury) to lower interest rates when old CBO rates are at least one percent above current rates.

—refinancing of loan guarantees every seven years when the Treasury lending interest rate exceeds the current Treasury rate by at least one percent and when the borrower requests it.
—requiring third party debt guarantees by the REA Administrator. This could insure that all cooperative borrowing is federally subsidized.
—requiring subordination of Government first lien status—risking billions in Government assets.
—including broader criteria for the special (2 percent) interest rate on insured loans.

Instead of accepting S. 1300, I propose that the President's 1985 budget proposal be adopted to reduce Federal risk and encourage more private sector involvement by:

—reducing existing Government loan levels over time and requiring co-ops to increase private borrowing;
—reducing the Federal share in rural electric and telephone funding (a Lehman Brothers' report concludes that the co-ops can significantly increase private sector borrowings to meet financial needs); and
—encouraging, through these actions, major improvements in REA borrower balance sheets so that they could at least operate in a more businesslike environment with less, not more, Government dependence.

As Secretary Block has previously discussed with you, the Administration believes that a strong, healthy rural electrification program remains important to insuring the economic health and quality of life of rural areas. But S. 1300 represents a grossly inequitable effort to use taxpayer dollars to provide special benefits to private business interests that have organized a massive pressure campaign. Were it to pass in its current form, I would not hesitate to recommend that the President withhold his approval of the bill.

The Administration looks forward to working with the Congress to deal effectively with the revolving fund problem over the next few years.

Sincerely,

DAVID A. STOCKMAN, *Director.*

COST ESTIMATE

I.

In accordance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate, the Committee estimates that enactment of S. 1300 would increase Federal outlays by an estimated $9.3 billion over the fiscal years 1985 through 2010, with most of the budgetary effect occurring after 1990. In the short term, increased interest receipts and reduced interest paid to the Treasury on certificates of beneficial ownership would reduce net Federal outlays by about $228 million over the 1985 through 1989 period. These estimates are based on the cost estimate prepared by the Congressional Budget Office.

II

In accordance with the Congressional Budget Act of 1974, the Congressional Budget Office prepared the following cost estimate:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, June 21, 1984.

Hon. JESSE A. HELMS,
Chairman, Committee on Agriculture, Nutrition and Forestry, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the attached cost estimate for S. 1300, the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984.

If you wish further details on this estimate, we will be pleased to provide them.

Sincerely,

RUDOLPH G. PENNER, *Director.*

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

1. Bill number: S. 1300.

2. Bill title: The Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984.

3. Bill status: As ordered reported by the Senate Committee on Agriculture, June 7, 1984.

4. Bill purpose: This bill amends the Rural Electrification Act of 1936, as amended, for the purpose of improving the financial condition of two off-budget revolving funds administered by the Rural Electrification Administration (REA): the Rural Electric and Telephone Revolving Fund (RETRF), and the Rural Telephone Bank (RTB). It also expands the forms of assistance to electric and telephone cooperatives under these REA programs.

Sections 4 and 6 provide additional resources to the revolving fund. Section 4 repeals the fund's obligation to repay $7.9 billion owed to the Treasury starting in 1993. Section 6 establishes a formula for setting interest rates charged to borrowers such that the interest from future loans made in a given period will equal—but not exceed—the interest expense on obligations incurred by the fund in the same period. The bill further specifies that this rate shall be sufficient to produce interest income equal to the interest expense on all of the RETRF's outstanding obligations, but no less than the existing statutory rate of 5 percent. Section 6 also revises the eligibility criteria for "special rate" loans, which are to bear interest at no more than one-half of the standard rate, but no less than the existing rate of 2 percent. It creates a reserve to cover some of the cost to the fund from special rate loans, and directs the Secretary of Agriculture to request appropriations for any costs not covered by the reserve.

S. 1300 also affects interest received by the Federal Financing Bank on certificates of beneficial ownership (CBOs) and on loans made to electric and telephone cooperatives. Section 5 authorizes the REA Administrator to repurchase CBOs, without penalty, after obtaining the approval of the FFB. These notes may be refinanced whenever the interest rate on a CBO exceeds the current rate for

similar issues by 100 basis points. Likewise, Section 7 authorizes lenders, including the FFB, to refinance REA-guaranteed loans, without penalty, if a loan's remaining maturity exceeds seven years and the interest rate exceeds the current rate by more than 100 basis points.

S. 1300 makes several forms of REA assistance mandatory rather than discretionary. Section 6 requires the Administrator to make special rate loans for all borrowers that satisfy the eligibility criteria. Section 7 requires the Administrator to guarantee loans made by other lenders for the purposes of improving the financial strength and stability of the borrowers. Section 7 also requires the Administrator to accommodate or subordinate the government's security on loans made or guaranteed by the REA upon the request of the borrower, if the Administrator determines that the borrower's revenues will be sufficient to repay its indebtedness and that the government's security will not be jeopardized. Section 8 specifies that if the minimum loan level for electrification borrowers in any year is less than $1.0 billion, the ratio that determines the amount of supplemental financing shall be fixed at the ratio in effect for 1983.

S. 1300 directs the REA to issue rules and regulations implementing the new interest rate formulas and the lien accommodation and subordination policies. The bill also requires the creation of separate accounts for the electric and telephone revolving funds.

In addition, S. 1300 includes a number of provisions affecting the Rural Telephone Bank (RTB), a supplemental source of financing for rural telephone companies. It removes the current 1991 time limit on U.S. government purchases of Class A stock in the bank. It also removes certain procedural and eligibility barriers to borrowing from the RTB.

5. Estimated cost to the Federal Government: Relative to current law, and under the economic assumptions used in this analysis, enactment of S. 1300 would increase federal outlays by an estimated $9.3 billion over the fiscal years 1985 through 2010. Most of these budgetary effects would occur after 1990.

Over the next five years, the budgetary impacts are expected to result from an increase in interest receipts from borrowers. The additional interest income would reduce the volume of CBOs sold to the FFB to finance new loans, which in turn would reduce the amount of interest paid to the Treasury for those borrowings. It is estimated that these transactions would reduce net federal outlays by about $228 million over the 1985–1989 period. The following table summarizes the bill's impact, both on- and off-budget, for the fiscal years 1985 through 1989.

[By fiscal years, in millions of dollars]

	1985	1986	1987	1988	1989
Effect on the unified budget:					
Estimated budget authority			3	9	20
Estimated outlays			3	9	20
Off-budget effect:					
Estimated budget authority		−19	−55	−83	−103
Estimated outlays		−19	−55	−83	−103
Net outlays (on- and off-budget)		−19	−52	−74	−83

Sections 5 and 7, which authorize the refinancing of CBOs and REA-guaranteed loans, also could have significant potential budgetary effects. Such refinancing would depend on the FFB's willingness to exercise this authority. If the FFB allowed the REA to refinance CBOs, federal outlays would increase by an estimated $1.0 billion over the 1985–2010 period. Likewise, if the FFB allows eligible borrowers to refinance guaranteed loans, the loss of interest and penalty payments to the government could total about $0.1 billion through the year 2010. Neither of these potential effects are included in the above table, because it is assumed that the FFB would not approve such refinancing.

The costs of this bill fall within budget function 270.

Basis of estimate

For the purposes of this analysis, the Congressional Budget Office assumes that the bill will be enacted by August 1984. It is assumed that obligations of the RETRF will continue to be funded by principal repayments, interest income, and from the sale of loan assets to the FFB in the form of CBOs. The level of loans made and guaranteed by the RETRF is assumed to be consistent with the minimum levels specified by the Congress for fiscal year 1984, as adjusted for inflation in future years. The inflation and interest rate assumptions used in this analysis are based on the assumptions in the baseline projections for fiscal year 1985. (The long-term interest rate on Treasury debts is assumed to be 11.4 percent in 1985, declining to 10.6 percent in 1989 and thereafter. The annual rate of inflation is assumed to be about 4 percent.) This estimate reflects the impact of the bill for both the electric and telephone programs, relative to current law.

Applying these assumptions, the RETRF's asset portfolio under current law would be exhausted by the year 2002 if lending continues at current levels (adjusted for inflation). If the fund exhausts its assets, it would default on some of its obligations to either the Treasury of the FFB. The Congressional Budget Office assumes that, under current law, REA would prevent such a default by reducing lending by the amount needed to ensure that the fund's resources would be sufficient to cover its obligations. For the base case, the Congressional Budget Office estimates that REA would need to reduce loan commitments by 1990. Thus, under current law, receipts to the RETRF would exceed new obligations through the year 2010, because of this anticipated decline in lending. Income from borrowers would be used to repay the RETRF's obligations to the FFB and the Treasury instead of being re-loaned to cooperatives.

The resources provided by S. 1300 would enable the REA to maintain current lending levels (as adjusted for inflation) over the 1985–2010 period. Net federal outlays are estimated to increase by $9.3 billion through the year 2010 as a result of this increased lending activity.

This estimate assumes that the standard interest rate would be set so that the interest payments from the 35-year amortized loans to borrowers would equal the fund's interest payments on the 30-year, non-amortized obligations to the FFB. In addition, the Administrator is expected to impose an interest surcharge on loans so that interest income from borrowers will equal the interest expense on all of the fund's obligations. For this estimate, it is assumed that a surcharge would be applied when the balance between the fund's interest expense and interest income requires an infusion of money. Under the assumptions used in this analysis, the standard rate would average 8.5 percent over the 1985–2010 period.

Approximately 60 electric borrowers are expected to qualify for the mandatory special rate loans. It is estimated that a total of $0.2 billion would be appropriated through the year 2010 to cover the cost of special rate loans not covered by the reserve.

Enactment of the provisions in Section 7 regarding lien accommodation and subordination would dilute the government's security on loans made or guaranteed by REA, and increase the risk of loss to the government in the event of default. The budgetary effects of such lien accommodations or subordinations cannot be estimated accurately, because of the uncertainty regarding the Administrator's determinations and the risk of defaults. However, the volume of outstanding loans potentially subject to lien accommodation or subordination totaled $23.3 billion by the end of fiscal year 1983.

Entitling electric and telephone borrowers to REA loan guarantees and the associated loans from the FFB is not expected to significantly affect the REA's contingent liability or FFB outlays, because virtually all such loans are guaranteed in any event.

Other provisions of the bill are not expected to have a significant budget impact.

6. Estimated cost to state and local governments: Enactment of this bill may affect the costs of service for the 20 municipal utilities that are eligible for REA loans and loan guarantees. For example, the provision in Section 7 requiring the Administrator to guarantee loans may reduce the interest rate on the tax-exempt bonds issued by these municipal utilities for electric or telephone facilities. The bill also could reduce costs if the municipal utility is eligible for special rate loans.

7. Estimate comparison : None.

8. Previous CBO estimate: On December 9, 1983, the Congressional Budget Office prepared an analysis of H.R. 3050, as ordered reported by the House Committee on Agriculture. The differences between that estimate and the estimate of S. 1300 are due to differences in the bills' provisions and in the economic assumptions used in the analyses.

On April 12, 1984, CBO prepared an analysis of S. 1300, as introduced, for the Subcommittee on Agricultural Credit and Rural Electrification of the Senate Committee on Agriculture, Nutrition, and Forestry. The differences between that analysis and this estimate reflect the Committee amendments to the bill.

9. Estimated prepared by: Kathy Gramp.

10. Estimate approved by: C. G. Nuckols (for James L. Blum, Assistant Director for Budget Analysis).

Regulatory Impact Evaluation

In compliance with paragraph 11(b) of rule XXVI of the Standing Rules of the Senate, the Committee makes the following evaluation of the regulatory impact that would occur in carrying out S. 1300, as reported by the Committee.

The purpose of the bill is to amend the Rural Electrification Act of 1936 to ensure continued access to federally-provided loan programs for rural electric and telephone cooperatives and companies. This purpose would be accomplished through (1) the conversion to equity capital of the Rural Electrification and Telephone Revolving Fund of certain notes issued by the Rural Electrification Administration to the Treasury, (2) the implementation of new interest rate-setting mechanisms which would increase the interest rates that most borrowers must pay on moneys borrowed from the revolving fund, (3) the requirement that the Secretary of Agriculture request appropriations to compensate for costs (in excess of a reserve established by the Administrator of the Rural Electrification Administration) that are attributable to "special" rate loans, and (4) the authorization of the Administrator, with the approval of the Federal Financing Bank, to repurchase outstanding certificates of beneficial ownership under certain circumstances when their interest rates exceed the current interest rate by at least 1 percent. Additional provisions of the legislation would require the Administrator to accommodate or subordinate liens or mortgages for purposes of encouraging borrowers to obtain credit from non-Government sources, expand the definition of 'rural area" used in the telephone loan program, and freeze the current loan criteria and ratios applicable to supplemental financing obtained in connection with insured electrification loans when the level of REA electrification loans is set by law at less than $1 billion annually.

As of September 30, 1983, there were 1007 active borrowers under the telephone loan program and 993 active borrowers under the electrification loan program (930 electric distribution cooperatives and 63 generation and transmission systems). The outstanding loans made to these borrowers from the revolving fund total approximately $12.9 billion. An additional $20.2 billion in loans made by non-REA sources (primarily the Federal Financing Bank) is guaranteed by REA.

The bill is not a regulatory measure in the sense of imposing Government standards or significant economic or regulatory responsibilities on the private sector. The programs affected by the bill are loan programs that provide funds in the form of insured or guaranteed loans for the purpose of providing electric or telephone service to rural areas.

Because the assistance authorized under these programs is provided in the form of loans, loan applicants must meet certain requirements and must submit detailed financial information concerning their operations. However, the programs are voluntary for these applicants and the information required of both applicants and borrowers is the same kind of information that is required by other lenders for similar purposes. The amount of paperwork involved in processing loan applications and servicing loans is comparable to that required by commercial lenders. Any additional regu-

latory burdens on borrowers will be minimal, since virtually all information needed to carry out the proposed legislation is already collected by REA.

The proposed legislation would have very little additional impact on personal privacy since the programs, as they presently exist, require disclosure of the same information as would be required under the bill.

ADDITIONAL VIEWS OF SENATORS HUDDLESTON, COCHRAN, ZORINSKY, ANDREWS, MELCHER, BOSCHWITZ, PRYOR, JEPSEN, BOREN, DIXON, AND HEFLIN

We are pleased that the Committee on Agriculture, Nutrition, and Forestry is reporting S. 1300, the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984, to the Senate with the recommendation that it pass. This far-reaching legislation addresses one the most critical issues before Congress this year and is an essential effort to hold down the upward pressure on rural utility rates.

S. 1300, as reported, will amend the Rural Electrification Act of 1936 to ensure that the Nation's rural electric and telephone systems will be able to continue to provide high quality, affordable electric and telephone service to consumers in rural America.

A major source of financing for rural electric and telephone systems—the Rural Electrification and Telephone Revolving Fund administered by the Rural Electrification Administration—is in jeopardy. The solvency of the fund is threatened because of the high interest rates in recent years.

Action by Congress is needed to make the revolving fund self-sustaining and otherwise enable the rural electric and telephone systems to obtain adequate financing at a reasonable cost for their operations.

Without legislation to strengthen the fund and improve the operation of the Rural Electrification Administration loan programs, in the near future there will be only two options: provide huge amounts of tax dollars each year to bail out the fund or greatly increase the cost of financing for many rural electric and telephone systems.

The most reasonable solution to the problem is the approach taken by S. 1300. That legislation represents a combined effort on the part of the Federal Government and the Rural Electrification Administration borrowers, who will contribute $11.1 billion in the form of higher interest rates, to resolve the problem in a cost-effective and equitable fashion.

Background on the Rural Electrification and Telephone Revolving Fund

To understand the operations of the Rural Electrification and Telephone Revolving Fund, it is necessary to review the fund's original and the model on which it was based.

On December 29, 1972, the Department of Agriculture announced that beginning on January 1, 1973, the Rural Electrification Administration would no longer make direct rural electric and telephone loans. Instead, the Department said it would use the broad community development authorities provided under the Rural De-

velopment Act of 1972 to make insured and guaranteed loans to electric and telephone systems. At the same time, $455 million in unobligated loan funds that had been appropriated by Congress were impounded.

In response to the Department of Agriculture's actions, Congress proceeded to develop amendments to the Rural Electrification Act providing for a Rural Electrification and Telephone Revolving Fund patterned after the Rural Development Insurance Fund.

These amendments were enacted as Public Law 93-32 on May 11, 1973. The 1973 legislation established the Rural Electrification and Telephone Revolving Fund, and provided it with initial capital by transferring to the fund the following assets:

Outstanding notes payable by electric and telephone borrowers to REA	$6,598,683,958
Undisbursed balances of electric and telephone loans	882,132,617
All collections of principal and interest from borrowers after June 30, 1972	261,964,343
Other assets, including appropriations for interest subsidies and losses made by Congress	60,000,000
Total assets	7,802,780,918

At the same time, the 1973 legislation made the revolving fund liable for $7,408,638,673 of notes issued by the Rural Elecrification Administration to the U.S. Treasury from August 14, 1953, through March 19, 1973, for amounts borrowed from the Treasury to make advances on the outstanding loans to utility borrowers. With assets of $7.8 billion and liabilities of $7.4 billion, the revolving fund was started with a net worth or equity investment by the Government of $400 million (only 5 percent of its assets).

The 1973 legislation provided that the fund's assets would be used for payment of the outstanding Treasury notes (without interest) on their original maturity dates (which range from June 30, 1993, through December 31, 2012), as well for the operation of the REA insured loan programs. The 1973 legislation also directed the Secretary of the Treasury to purchase any new notes issued by the revolving fund to discharge obligations of the fund.

In 1974 and 1976, two additional notes were issued totaling $455 million. These notes also became liabilities of the fund, bringing the total amount of long-term notes payable by the Rural Electrification Administration to the Treasury to $7,864,742,067. These notes are attributable to each of the electric and telephone programs as follows:

	Amount	Percent
Electric	$6,028,195,224	76.6
Telephone	1,836,546,843	23.4
Total	7,864,742,067	100.0

Under the 1973 legislation, collections of principal and interest on the outstanding notes that initially capitalized the fund are used to make advances to borrowers and pay interest on the fund's obligations. These collections, supplemented by the undisbursed

balances of notes to the Treasury, were sufficient to cover advances to borrowers through fiscal year 1975.

However, beginning in fiscal year 1976, the Rural Electrification Administration found it necessary to use the authority provided by the 1973 legislation to issue new obligations—in the form of certificates of beneficial ownership (CBO's)—to the Federal Financing Bank to raise cash to meet the needs of the fund in excess of collections on outstanding loans.

A CBO is a special type of bond used by Federal lending agencies to borrow from the treasury through an agency of the treasury, the Federal Financing Bank. To cover certain administrative expenses, the Federal Financing Bank charges the Rural Electrification Administration an interest rate for CBO's that is one-eighth of one percent above the treasury cost of borrowing.

As used by the Rural Electrification Administration, a CBO evidences the sale of new notes in the revolving fund's inventory of notes representing the Rural Electrification Administration loans to rural utilities under a trust agreement whereby the revolving fund promises (a) to pay interest to the Federal Financing Bank, the purchaser of the CBO, at a stipulated rate not necessarily the same as (and, in the case of the Rural Electrification Administration CBO's to date, higher than) the interest rate specified in the utility borrowers' notes to the Rural Electrification Administration, and (b) to repurchase the CBO at its maturity date.

CBO's enable the Rural Electrification Administration to resolve cash flow problems that result when receipts to the revolving fund are insufficient to cover interest expenses and make loans at the program levels set by Congress in appropriation acts. The interest costs on these CBO's have ranged from 8.1 percent to 15.3 percent. CBO's issued to date total $3,467,507,000 and carry an average interest rate of 11.394 percent.

Over the past several years, the large gap between the standard 5 percent rate of interest that the Rural Electrification Administration is required by law to charge its rural utility borrowers for insured loans and the higher Treasury rate for CBO's paid by the Rural Electrification Administration to obtain funds has severely eroded the financial stability of the revolving fund.

Need for the Legislation

During the hearings on S. 1300, the individuals and organizations interested in maintaining the rural electric and telephone programs of the Rural Electrification Administration all agreed on one important point: the the Rural Electrification and Telephone Revolving Fund, through which many rural utility systems receive their financing, is in serious financial trouble and action by Congress is needed to resovle the problem.

For example, Harold Hunter, Administrator of the Rural Electrification Administration, while expressing reservations about S. 1300, testified that he was pleased Congress and the trade associations have "heeded the alarms we have sounded over the past several years concerning the deteriorating financial condition of the Rural Electrification and Telephone Revolving Fund".

Rudolph G. Penner, Director of the Congressional Budget Office, testified that without congressional action the revolving fund's financial problems will cause the REA insured loan programs, operated through the revolving fund, to be shut down. In the absence of appropriations or legislation like S. 1300, Mr. Penner testified, the REA loan programs must be terminated within the next few years because the revolving fund will lack the assets to make new loans.

Anthony J. Gabriel, Deputy Inspector General of the Department of Agriculture, testified that the interest expenses of the revolving fund will exceed interest income by the second half of fiscal year 1985 and that appropriations will be needed to cover the shortfall.

It is clear from the testimony presented on S. 1300 that, if Congress does not act, the assistance provided through the Rural Electrification Administration revolving fund will be terminated and the financing costs or rural utilities will sharply escalate. Higher financing costs will put additional upward pressure on rural utility rates.

On the average, consumers in rural areas already pay higher utility rates than city dwellers because of the high cost of providing electric and telephone service in areas of low population density. Recent evidence of this was disclosed during the hearings when a REA internal memorandum dated November 1, 1983, was made part of the hearing record. The memorandum is included in these additional views as appendix A.

The memorandum indicates that 68.7 percent of the Rural Electrification Administration electric utility borrowers charge rates that are higher than comparable (as defined by the Department of Energy) investor or publicly-owned utilities. Further, the memorandum indicates that a trend has been established whereby each year fewer Rural Electrification Administration borrowers are able to charge rates that are below the rates charged by comparable investor or publicly-owned utilities.

It is difficult to analyze differences between rural and urban telephone rates. In many cases, the actual cost of basic service is similar but, while urban dwellers may have area free calling that encompasses hundreds of thousands of residents and businesses, rural citizens frequently pay toll charges for calls to local schools or doctors. In addition, the quality and variety of services that are considered standard and essential in urban areas are not always available in rural areas.

Out of a concern about the economic consequences for rural America if the Rural Electrification Administration insured loan programs are ended, numerous organizations and individuals—including three former Administrators of the agency—have carefully studied the possible solutions to the financial problems of the revolving fund. After an extensive examination of the problems, these organizations, including the National Rural Electric Cooperative Association, the National Telephone Cooperative Association, the National REA Telephone Association, the National Rural Utilities Cooperative Financing Corporation, and the Power and Communication Contractors Association, have concluded that a responsible and equitable solution to the problems must include a significant contribution from all parties to ensure the stability of this essential source of financing.

For that reason, those organizations have given their unqualified endorsement to S. 1300, legislation that addresses the financial problems of the REA revolving fund by increasing interest rates on loans made to rural utilities from the fund and strengthening the capital base of the fund by reclassifying $7.9 billion in notes, due to the U.S. Treasury beginning in 1993, as equity capital of the fund.

Cost of Maintaining the Rural Electric and Telephone Insured Loan Programs

The Congressional Budget Office estimates that S. 1300, as reported, would increase budget outlays by $9.3 billion over 25 years. However, that estimate, while using standard budgetary procedures, is based on the unlikely supposition that, without enactment of S. 1300, Congress will not take other action to avert the termination—in the very near future—of the REA rural electric and telephone insured loan programs.

We strongly believe that Congress should, and will, take action to maintain the essential Rural Electrification Administration insured loan programs. This can be accomplished through either the approach taken by S. 1300, that is, strengthening the revolving fund, or—the other most likely alternative—appropriations. Between those two alternatives, S. 1300 will ultimately reduce the Federal deficit because if it is not enacted—and the insured loan programs are to continue operating as they do today—Congress will have to appropriate funds that will far exceed the cost of S. 1300.

The potential high cost of maintaining the present Rural Electrification Administration programs through appropriations in future years is one of the strongest arguments in support of S. 1300. On June 4, 1984, in response to questions that were raised during the hearings on S. 1300, the Congressional Budget Office estimated that through the year 2010 it could cost up to $17 billion to maintain the present REA electric and telephone insured loan programs through appropriations. The Rural Electrification Administration estimates that the cost of appropriations would be $30 billion through the year 2017. That estimate is reproduced in appendix B of these additional views.

Although the cost of resolving the problem under S. 1300, as introduced, is substantially less than the cost involved in using appropriations, the Committee adopted two amendments to S. 1300 proposed by Senator Huddleston to further reduce the potential cost of S. 1300.

The first amendment requires that the revolving fund be managed in such a way as to be balanced, that is, interest income must, at all times, equal the interest expenses of the fund. The General Accounting Office, the Congressional Budget Office, and the administration all acknowledge that the amendment reduces the cost of the legislation. According to the Congressional Budget Office, the savings could be as high as $1.5 billion.

The second amendment requires that the President of the Federal Financing Bank (the Secretary of the Treasury) give his approval before certificates of beneficial ownership held by the Federal Financing Bank may be refinanced. As discussed in greater detail

above, CBO transactions are used by the Rural Electrification Administration to obtain supplemental funds to finance its loan programs. CBO transactions are similar to loans, in that they require interest payments to the Federal Financing Bank and eventual repurchase of the CBO's by the Rural Electrifiction Administration.

The amendment addresses the administration's concern that if interest rates come down, under S. 1300 as introduced, the Rural Electrification Administration would refinance CBO's that bear high interest rates even though the Federal Financing Bank might have to continue paying higher interest rates on the money it borrowed to buy the CBO's. The Congressional Budget Office estimates that the amendment will save about $1 billion.

Much of the Committee's debate about this legislation has focused on the cost to the Government of the various proposals. Under S. 1300, however, the balancing of the Rural Electrification Administration revolving fund will be a joint effort with borrowers and, therefore, the 25 million consumers served by Rural Electrification Administration-financed utilities. The Congressional Budget Office estimates that the contribution made by Rural Electrification Administration borrowers in the form of higher interest rates will be about $11.1 billion under S. 1300, as reported. That estimate is included in these additional views as appendix C. The combined effort on the part of the Federal Government and REA borrowers will make it possible for the fund to become permanently self-sustaining.

Committee Consideration of Alternatives to S. 1300

During the Committee's markup of the legislation, the Committee considered not only S. 1300, but also the relevant provisions of current law, the House-passed companion bill to S. 1300 (H.R. 3050), a bill introduced by Senator Simpson (S. 2646), and the administration's legislative proposal, which was submitted on April 11, 1984, but not introduced.

The Simpson bill is substantively the same as a proposal offered in the House of Representatives by Congressman Bethune of Arkansas. Congressman Bethune offered his proposal as an amendment in the form of a substitute for H.R. 3050, which the House rejected by a vote of 289 to 107.

During the Committee's markup, the advantages and disadvantages of the provisions of the Simpson-Bethune proposal (including those dealing with the interest rate formula and the handling of REA's notes payable to the Treasury) were reviewed.

Also, in the course of the markup, Frank Naylor, Under Secretary of Agriculture, and Harold Hunter, Administrator of the Rural Electrification Administration, were called on at various times to present the administration's views on the proposals before the Committee, including the administration proposal.

Although it is possible that the administration proposal and the Simpson-Bethune proposal could eventually balance the fund, the much higher interest rates and lower loan levels required under those proposals would create a severe burden for rural consumers. For that reason, the proposals were rejected.

After carefully considering each of the major provisions of the alternatives before the Committee, the Committee chose to report S. 1300 with several clarifying and strengthening amendments.

S. 1300, as amended, was ordered reported with only a single dissenting vote.

Explanation of the Key Provisions of S. 1300, As Reported

Providing the revolving fund with equity capital

Section 4 provides that $7.9 billion in notes issued by the REA Administrator to the Secretary of the Treasury in return for funds for REA's rural electrification and the telephone operations "shall be equity capital of the fund" instead of "liabilities of the fund".

This provision to exchange Rural Electrification Administration notes to the Treasury for equity interests in the fund will strengthen the fund by reducing the fund's need for new borrowing through the sale of certificates of beneficial ownership (CBO's). It is important to realize that, unless the revolving fund is restructured, the Rural Electrification Administration will have to issue additional CBO's or new notes to meet the repayment schedule on the $7.9 billion in original capital.

It is clear that the continued, and increasing, use of CBO transactions to keep the revolving fund operational and maintain the present Rural Electrification Administration electric and telephone programs is not a feasible alternative without massive appropriations to cover the costs of using CBO's.

As explained in greater detail above, CBO's are issued by the Rural Electrification Administration to resolve cash flow problems that result when receipts to the revolving fund are insufficient to cover interest expenses and make loans at the program levels set by Congress in appropriation acts.

The use of CBO's to obtain funds to loan through the Rural Electrification Administration revolving fund is not an unusual arrangement. The Farmers Home Administration and other agencies issue CBO's. However, other revolving funds also receive an appropriation every year to cover the differnece between interest received from borrowers and interest paid to the Treasury. Although the 1973 Rural Electrification Administration legislation authorized Congress to make appropriations for interest subsidies and losses to keep the revolving fund viable, fiscal year 1984 was the first year an appropriation was made for that purpose.

For fiscal year 1984, an appropriation of $197,862,000 was made to reimburse the Rural Electrification and Telephone Revolving Fund for the differential between interest income and interest expenses on loans made during fiscal year 1982. Appropriations must continue each year at ever increasing levels if the present insured loan programs are to continue and legislation similar to S. 1300 is not enacted.

For fiscal year 1984, the appropriations for interest and other losses of other revolving funds are as follows:

(FmHA Rural Housing Insurance Fund	$1,508,082,000
(FmHA) Agricultural Credit Insurance Fund	895,522,000
(FmHA) Rural Development Insurance Fund	477,829,000
(REA) Rural Communication Development Fund	375,000

The Congressional Budget Office estimates that, assuming current loan levels, the use of appropriations to place the revolving fund on a sound financial basis could cost as much as $17 billion between 1985 and 2010. The Rural Electrification Administration estimates that, under present law, the cumulative appropriations needed to cover interest subsidies may total $30 billion during the period of the scheduled Treasury note retirement, 1993 through 2017. That estimate is reproduced in appendix B of these additional views.

The Committee has determined there is a better and less costly solution to balancing the revolving fund, a solution that can, and should, be implemented immediately. Part of this solution is to give the Rural Electrification Administration the authority to make periodic adjustments of interest rates charged for loans to its rural utility borrowers, as provided for in S. 1300, to better enable the Rural Electrification Administration to cover the expenses of the fund.

To help offset the adverse effects that higher interest rates would have on the cost of utility service to rural residents, and to permanently strengthen the revolving fund, the Committee has also chosen to allow the continued use by the fund of the $7.9 billion of original capital. We believe that it is appropriate and desirable that the original capital invested in the fund by the Federal Government be reclassified as Government equity so that it can remain in the fund for as long as is needed to ensure that the purposes of the Rural Electrification Act are achieved.

Some opponents of the legislation have tried to characterize the reclassification provision as a "forgiveness". This is simply not the case. The fact is, such conversions of debt to equity are common in business and are considered prudent investment decisions.

Frequently, investors holding bonds with conversion features exercise their option to convert bonds into equity in the form of stock. These individual investors have not given anything away nor given up control of their investment. The same will be true for the Federal Government under S. 1300. The revolving fund and its assets will remain under the direct authority and control of the Government. If at some future time the need for REA lending should cease, all assets and income of the fund would automatically revert to the Treasury.

Further, we believe such a continued commitment of resources will have a positive effect on the national debt since the amount of appropriations needed for interest subsidies authorized under present law—and provided routinely to other revolving funds—would greatly exceed the amount of non-interest bearing notes exchanged for equity interests in the fund under S. 1300.

AUTHORIZING REPURCHASE OF CBO'S WITHOUT PENALTY

Section 5 authorizes the Administrator of the Rural Electrification Administration to repurchase outstanding CBO's, with remaining terms of seven or more years, from the Federal Financing Bank without penalty when their interest rate exceeds the current rate on new CBO's by one percentage point or more. S. 1300, as reported, incorporates an amendment requiring the approval of the Presi-

dent of the Federal Financing Bank (the Secretary of the Treasury) to refinance CBO's issued by the Rural Electrification Administration.

Although the Federal Financing Bank has been borrowing funds on a short-term basis to obtain the cash needed for long-term REA loans, the formula now being used for determining the amount needed to repay a CBO generally results in a penalty which discourages such prepayment. The ability to make prepayments of CBO's without such penalty could result in substantial savings of interest expenses to the revolving fund. The authority for prepayments, therefore, prvovides an additional tool for this and future administrations to use, if they so choose, to further strengthen the financial status of the fund if needed.

INTEREST RATES CHARGED TO REA BORROWERS

Section 6(1) directs the Administration to set and periodically adjust the standard rate of interest for new loans made to Rural Electrification Administration electric and telephone borrowers so that each of the electric and telephone accounts in the revolving fund will have interest income sufficient to cover its interest expenses. Under current law, the standard rate is 5 percent and cannot be adjusted.

Sections 6(1) and 6(3) revise the provisions regarding the special interest rate program for rural utility borrowers experiencing financial hardship.

S. 1300, as reported, incorporated two amendment relating to the interest rate provisions of the bill, as introduced.

The first amendment requires the Administrator to set the standard interest rates at levels that will ensure that each account in the fund is balanced.

The second amendment, proposed by Senator Zorinsky, requires the making of loans under the special interest rate program to borrowers that meet specified criteria and that are experiencing financial hardship. Under S. 1300, the special interest rate will be not less than two percent nor more than one-half the standard rate. To a large extent, the cost of this interest rate subsidy will be borne by all borrowers who receive loans through the revolving fund.

Periodic adjustment of the standard interest rate on loans from the revolving fund will save billions of dollars since future appropriations will not be needed to cover interest subsidies on standard rate loans.

The members of the various organizations supporting S. 1300 understand that this legislation will make the present standard interest rate of 5 percent for loans from the revolving fund a floor instead of a ceiling to cover the interest expenses on the fund's obligations. Rural electric and telephone systems will be paying these higher interest rates—which could easily be four times higher than the rate charged at the end of 1972 and 60 percent higher than the rate set in present law—for almost a decade before the first of the fund's non-interest bearing notes to the Trasury becomes due in 1993.

Rural electric and telephone systems can adjust to the higher and variable interest rates required under section 6(1) if the other program improvements provided under S. 1300 are also adopted.

EXPANDING LIEN ACCOMMODATION AUTHORITY

Section 7(2) requires the Rural Electrification Administration to accommodate and subordinate its liens or mortgages, at the request of rural utility borrowers, to enable the borrowers to obtain credit from other lenders for any purpose that would improve the efficiency, effectiveness, or financial stability of the borrower. However, accommodation or subordination will not be required unless the Administrator of the Rural Electrification Administration finds that the borrower has, or will have, the ability to repay its existing and proposed indebtedness.

In recent years, the Rural Electrification Administration has greatly curtailed the use of its funds an Rural Telephone Bank funds for certain purposes that have traditionally been financed by loans from those sources. Yet, borrowers have had difficulty obtaining funds for such purposes from other lenders because the Rural Electrification Administration is most reluctant to share its mortgage liens on satisfactory terms, even though the Goverment's interest is protected.

Further, agency loan agreements include an "after acquired clause" tht extends the Rural Electrification Administration's lien to all of a borrower's property owned or subsequently acquired by the borrower, even if the funds to acquire property were not provided by the Rural Electrification Administration or the Rural Telephone Bank. This clause is being used by the Rural Electrification Administration to impose conditions on boorrowers and lenders that discourage both from entering into commercial or cooperative financing arrangements.

If the purpose to be financed by the commercial or cooperative lender is a purpose that the Rural Electrification Administration claims it cannot finance under the Rural Electrification Act, the problem intensifies. In such cases, the Rural Electrification Administration generally demands a "compensating benefit" for sharing its lien with the commercial lender. Frequently, the compensating benefit demanded is a reduction in the term of existing loans or prepaying one or more loans. These conditions often make unattractive activities that would strengthen a borrower's overall financial position and actually enhance the Government's loan security.

In the past, the Rural Electrification Administration has been more flexible than it is today in providing lien accommodations without exacting a compensating benefit for purposes that it cannot finance. We believe that the obtaining of commercial financing that meets the standards set forth in the bill should, in itself, be considered as a satisfactory compensating benefit.

To protect the Government's interest, S. 1300 requires that before the Administrator can approve a lien accommodation or subordination, he must determine that the borrower will have the ability to repay all indebtedness. In making this determination, the Administrator will take into account not only physical assests but also projected revenues. It should be noted tht assigning a value to

projected revenues is not an unusual procedure in utility financing. The use of revenue bonds, secured solely by a system's proposed revenues, is the predominant method employed by many utilities, particularly those owned by government entities, to secure loans.

MAINTAINING 1983 SUPPLEMENTAL LOAN RATIOS FOR THE ELECTRIC PROGRAM

Section 8 provides that fiscal year 1983 criteria and ratios for supplemental financing under the Rural Electrification Administration electric program, which are also applicable for the current fiscal year, will be maintained in any fiscal year when the minimum insured loan level is established by law at less than $1 billion.

The supplemental loan ratios establish the amount of financing that an electric utility borrower must obtain from a source other than the REA revolving fund. Current law—and the provisions of S. 1300—set the supplemental financing ratio for most borrowers at 70/30. That is, for every 70 cents of insured loan funds obtained through the revolving fund, a borrower must obtain 30 cents from another source. The combined interest rates charged on the loans provide a composite interest rate for borrowers.

It is necessary to freeze the loan ratios at present levels because any increase in the amount of supplemental financing required would effectively increase the composite interest rate electric borrowers must pay. Since the interest rate provisions of S. 1300 increase interest costs for these borrowers, further increases through increased supplemental financing requirements would unduly burden the consumers served by the Nation's rural electric systems.

Under S. 1300, the important loan ratios currently in effect—and continued under the legislation—will not necessarily be forever fixed. For any year that the loan level of the insured electric loan program exceeds $1 billion, the Administrator will have the flexibility and authority to establish new ratios.

CONCLUSION

Although the challenge of bringing electricity and telephone service to rural areas has been successfully met by the Rural Electrification Administration programs, the job of the agency is not done. Like the utility systems in large cities where utility services have been available for decades, rural utility systems continue to need financing to replace obsolete facilities and equipment, extend service to new cuistomers, and repair damaged equipment. Without a viable revolving fund, as provided under S. 1300, for many rural utilities there will be no investment for the future and rural utility rates will have to be increased to prohibitively high levels.

S. 1300 provides as close to a permanent solution to the problem as can be achieved. Further, S. 1300 was introduced on May 17, 1983, which has given the administration and all those with an interest in this legislation a full year to review it and suggest alternative ways of addressing the problems of the Rural Electrification Administration revolving fund—which are growing progressively worse each day.

We believe that, given the length of time this legislation has been under review and the careful consideration the Committee gave to a full range of alternative solutions, it is appropriate that the Senate pass this legislation as soon as possible.

WALTER D. HUDDLESTON.
THAD COCHRAN.
EDWARD ZORINSKY.
MARK ANDREWS.
JOHN MELCHER.
RUDY BOSCHWITZ.
DAVID PRYOR.
ROGER JEPSEN.
DAVID L. BOREN.
ALAN J. DIXON.
HOWELL HEFLIN.

APPENDIX A

U.S. DEPARTMENT OF AGRICULTURE,
RURAL ELECTRIFICATION ADMINISTRATION,
Washington, DC, November 1, 1983.

Subject: Comparison of Residential Electric Rates at 1,000 kWh Usage per Month—REA Borrowers with Comparable DOE Data (January 1, 1983).

To: Joe S. Zoller, Assistant Administrator—Electric.

Through: Charles R. Weaver, Director, Electric Borrowers Management Division.

Enclosed is a listing by states and areas of the number of borrowers with electric rates for residential service at 1,000 kWh usage per month higher or lower than the comparable DOE utilities. Data are at January 1, 1983.

Reconciliation to the total population of distribution borrowers is:

	Number	Percent
REA borrowers are higher	631	68.7
REA borrowers are lower	288	31.3
Subtotal	919	100.0
Borrowers not submitting data	13	
Total population	932	

The number of borrowers with rates exceeding the DOE comparable utilities increased sharply, as had been projected. Comparison of Jan. 1, 1983, with the prior 2 years (excluding Alaska) shows:

[In percent]

	Jan. 1, 1983	Jan. 1, 1982	Jan. 1, 1981
REA borrowers are higher	68.4	53.5	52.2
REA borrowers are lower	31.6	46.5	47.8

We do not see a reversal in this negative trend of rate disparity at least for the next few years.

DAVID J. LESSELS,
Rate Policy Specialist,
Electric Borrowers Management Division.

REA BORROWERS RATE AT 1,000 kWh PER MONTH COMPARED TO DOE UTILITY AT JAN. 1, 1983

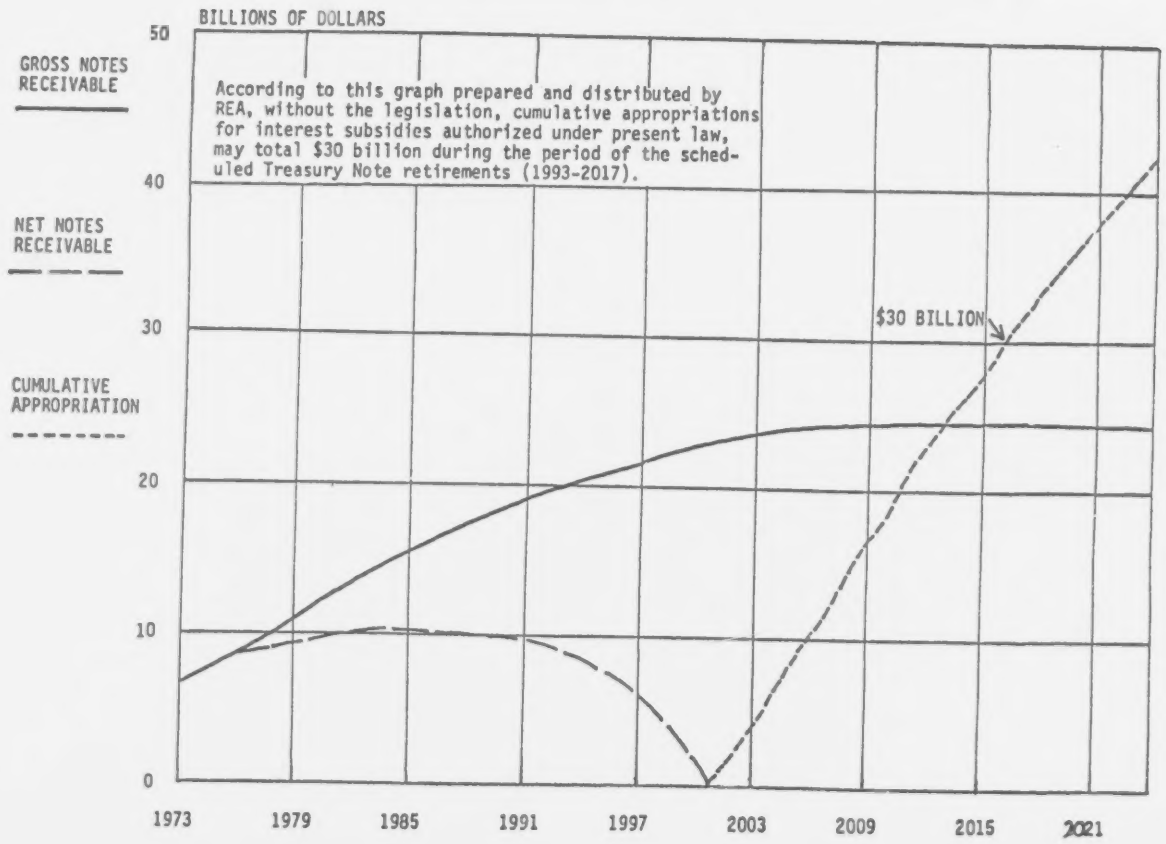
	REA is higher		REA is lower	
	Jan. 1, 1983	Jan. 1, 1982	Jan. 1, 1983	Jan. 1, 1982
Northeast area:				
Delaware	1	0	0	1
Indiana	6	5	35	36
Maine	4	3	0	1
Maryland	2	1	0	1
Michigan	13	3	0	0
New Hampshire	1	0	0	1
New Jersey	0	0	1	1
New York	0	0	4	4
North Carolina	19	7	9	21
Ohio	17	22	10	5
Pennsylvania	3	3	9	9
Vermont	1	0	1	2
Virginia	8	7	6	7
West Virginia	1	0	0	1
Total	76	61	75	90
Southeast area:				
Alabama	12	12	11	10
Florida	15	11	0	4
Georgia	41	29	1	14
Kentucky	26	26	0	0
Mississippi	10	12	13	11
South Carolina	12	2	8	18
Tennessee	23	23	1	1
Total	139	115	34	58
North Central area:				
Illinois	16	21	11	6
Iowa	37	22	11	26
Minnesota	30	22	18	26
North Dakota	11	3	10	18
South Dakota	11	10	21	22
Wisconsin	27	27	2	2
Total	132	105	73	100
Southwest area:				
Arizona	6	4	3	6
Arkansas	17	4	1	14
Louisiana	13	12	0	1
Missouri	23	11	18	30
New Mexico	9	6	7	9
Oklahoma	26	26	1	1
Texas	57	44	16	30
Total	151	107	46	91
Western area:				
Alaska	12	13	2	1
California	1	1	3	3
Colorado	12	6	10	16
Idaho	6	6	3	3
Kansas	23	16	12	19

REA BORROWERS RATE AT 1,000 kWh PER MONTH COMPARED TO DOE UTILITY AT JAN. 1, 1983—Continued

	REA is higher		REA is lower	
	Jan. 1, 1983	Jan. 1, 1982	Jan. 1, 1983	Jan. 1, 1982
Montana	11	10	13	14
Nebraska	28	26	4	6
Nevada	1	0	5	6
Oregon	14	10	0	4
Wyoming	11	11	3	3
Washington	13	11	2	4
Utah	1	0	3	4
Total	133	110	60	83

APPENDIX B

NOTES RECEIVABLE & CUMULATIVE APPROPRIATION



APPENDIX C

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, June 28, 1984.

Hon. WALTER D. HUDDLESTON,
Committee on Agriculture, Nutrition and Forestry, U.S. Senate, Washington, DC.

DEAR SENATOR HUDDLESTON: At your request, the Congressional Budget Office has estimated the amount of additional income paid by borrowers from REA over the 1985–2010 period, assuming current lending levels (adjusted for inflation in future years) and enactment of S. 1300, as ordered reported. We estimate that borrowers would pay about $11.1 billion more over that 25-year period under S. 1300 than if the same volume of loans were made at a 5 percent interest rate.

I hope that this information is helpful.

Sincerely,

RUDOLPH G. PENNER, *Director.*

ADDITIONAL VIEWS OF SENATOR PAULA HAWKINS

After presiding over a series of in-depth hearings and receiving testimony from 35 witnesses, including government officials, independent consultants, representatives of electric and telephone cooperative associations, business associations, and citizen groups, I wish to offer my thoughts on the problems experienced by the Rural Electrification and Telephone Revolving Fund. As a former Public Service Commissioner for the State of Florida and a former member of the Rural Telephone Bank Board, I can assure you that I firmly believe in and strongly support a continued and responsible Federal role in rural electric and telephone service. To jeopardize or hamper its effectiveness would be a tragic mistake which we simply cannot allow to happen.

The centerpiece of the rural electric and telephone programs is the Revolving Fund which was created in 1973 to assure that rural electric and telephone borrowers would have access to construction financing. This Fund was created with $7.9 billion in assets in the form of long-term notes to the Treasury, which the Fund was allowed to use interest-free. This has resulted in a substantial cost to the taxpayer according to the General Accounting Office. The assumption was that by relending the $7.9 billion at the modest rate of 5 percent, the Fund would operate sufficient "profits" to assure its viability as a perpetual source of financing, even after the interest-free $7.9 billion in principal was repaid to the Treasury. But instead, we have managed to threaten the long-term viability of the Fund after just a few years of operation. Simply put, the Fund has lent more money out annually than it has taken in, and has been forced to "finance" this cash flow shortfall by borrowng from the Treasury at rates substantially higher than the rates charged to Fund borrowers. This problem has been described by many as "borrowing high and lending low", with little attention to the true level of assistance required by individual borrowers. The majority of the witnesses testified before the Subcommittee that S. 1300 attempts to solve this problem by "forgiving" $7.9 billion in debts due the U.S. Treasury and slightly raising interest rates charged to borrowers. However, most of these same witnesses expressed concern that S. 1300 would not necessarily resolve the problem experienced by the Fund. I share their concern.

The cost of S. 1300 has been estimated by the Congressional Budget Office to be approximately $9.3 billion and estimated by other as high as $20 billion. It was also pointed out repeatedly during the hearings that the capitalization of the $7.9 billion in notes due the Treasury beginning in 1993 is actually a "forgiveness" since the Treasury will be forced to either increase tax revenues, reduce expeditures in other programs, or borrow in the credit markets to make up the shortfall. Further, several witnesses expressed grave concern about the precedent established by capitaliz-

ing the $7.9 billion, particularly in light of the approximately $135 billion in outstanding Federal Financing Bank (FFB) loans, which could fall victim to the same treatment.

In these comments, I will not dwell on the cost or treatment of the $7.9 billion, but instead focus on several proposed methods to resolve the Fund's problems which were presented to the Subcommittee. Additionally, I'll discuss the questionable practice of mandating that all borrowers receive at least 70 percent of their financing requirements from the Revolving Fund. To accomplish this, I will illustrate the wide divergence in characteristics of individual borrowers and how these characteristics actually affect their need to borrow from the Revolving Fund.

As stated during our hearings, one method to resolve the Fund's problem is to reduce the mandatory minimum loan levels established by Congress, so as to reduce the rapid drain on the Fund. These combined minimum loan levels currently stand at $1.1 billion per year for the electric and telephone programs. Unfortunately, if we significantly reduce these loan levels at this time, as some suggest, I fear that we may impair the effectiveness of the program. Until we better understand the actual needs of individual borrowers and have a better understanding of total program requirements, it is not possible to reduce these program levels without potentially creating hardships for some borrowers. As a result, I feel that a significant reduction in loan levels such as that proposed by the Administration would not be the proper course of action at this time.

An alternative method to resolve the Fund's problem is to raise interest rates charged electric and telephone borrowers so as to reduce the differential between the Fund's cost of borrowing from the Treasury and the cooperative's cost of borrowing from the Fund. This differential has exceeded eight percent in the recent past and varies with the cost of money to the government. During our hearings, several witnesses testified that if Congress sufficiently increased the interest rate charged to borrowers, it would not be necessary to either reduce program size or appropriate money to make up the Fund's shortfall. They also testified that there remains considerable financial leverage in the Fund which would allow the Fund to charge interest rates below the cost of borrowing from the Treasury while continuing to provide for the solvency of the Fund. For this reason, I believe the Administration's proposal to charge interest rates equal to the cost of borrowing by the Treasury is unnecessary and could place an undue hardship upon many borrowers.

In addition, it was pointed our during the hearings that S. 1300, even with the Stenholm Amendment, might not ensure the permanent solvency of the Fund. While it is estimated that this proposal would result in rates initially averaging approximately 8.5 percent, rates would eventually increase up to and possibly exceed the cost of money to the government. And according to the Congressional Budget Office, S. 1300 as amended, could create volatile interest rates as well. For these reasons, I am concerned that the interest rate formula contained in S. 1300 contains too many unanswered questions and I believe that further modifications in this interest rate formula may be necessary to ensure the solvency and stability

of the Fund. Without some modification to the formula, the Fund's borrowers face an uncertain future.

Another proposal, S. 2646, would effectively raise interest rates charged to borrowers through the use of a different formula. Because of the remaining leverage in the Fund, interest rates derived using the S. 2646 formula, would still be significantly lower than the Government's cost of borrowing, yet would allow for the repayment of the Fund's debt to the Treasury. Thus, the question becomes—do we charge S. 1300 rates which may not even assure the solvency of the Fund, or do we charge the additional percent or two which would be needed to permit the Fund to repay its obligations to the Treasury and remain as a permanent financing source? It has been estimated by some, that choosing the latter would increase average residential electric bills by only a penny a day more than the increase afforded in S. 1300. If this is correct, I believe we should take a closer look at S. 2646.

A third alternative for resolving the Fund's problems is for Congress to make direct appropriations to make up for the shortfall between loans made by and income received by the Fund. Several witnesses testified that if Congress chose to appropriate this shortfall each year, more attention would be focused on the true cost of this off-budget program. However, Congress has already recognized the Fund's dilemma and appropriated $197 million last year and appears to be ready to appropriate even more for next year. These appropriations have had the additional benefit of buying us additional time before the fund begins to suffer the depletion of its assets. However, in the long run, I don't believe Congress wants to make direct appropriations every year. I believe a more appropriate and responsible approach would be to address the interest rate issue and make other modifications in the program.

Notwithstanding the technical problem of keeping the Fund solvent, there is another issue which is becoming more and more important in these times of limited government resources and extreme pressures on our financial markets. This issue is one of FAIRNESS—fairness to noncooperatives residents as well as fairness among the various cooperatives and their consumers. Almost 50 years ago, Congress made the conscious decision to establish a program which would provide loan funds, without subsidy, to rural Americans who otherwise would not have been afforded telephone and electric service. What I am concerned about is that, with 99 percent of our farms electrified and with 95 percent of our farms receiving telephone service, we still largely treat all borrowers alike, regardless of their particular financial situation or the characteristics of their consumers. In effect, this program has become what some might call an entitlement for borrowers, with each electric borrower guaranteed at least 70 percent of its financing from the federal government through the Revolving Fund. The only criteria for continued eligibility is that borrowers were rural in nature when formed. Unfortunately, little attention is paid to the characteristics of the individual borrowers and how these characteristics may have changed since their formation. We can review a number of examples to see how cooperatives which have gained a degree of financial stability and which have favorable rate struc-

tures have continued to borrow from the Fund at the expense of other borrowers.

Some of the testimony we have received in support of S. 1300 suggests that rural electric cooperatives tend to have higher electric rates than their investor-owned utility (IOU) counterparts. In fact, according to the General Accounting Office, 681 out of 921 cooperatives studied have electric rates lower than the average IOU residential rate and 280 of them had rates more than 21 percent lower. When reviewing the special low rate 2 percent borrowers, the General Accounting Office found that some 61 percent of them already had lower rates than their neighboring investor owned utilities, yet were still allowed the special low rate due to the current density criteria. These low-rate loans place an additional strain on the Revolving Fund and, thus, place an additional burden upon the remaining borrowers who may have higher rates than their neighboring IOU's. The question to be asked is, "Is this really fair?" Is it really fair to those cooperatives with higher rates than their neighboring utility? Is it really fair to all other cooperatives to continue this depletion of the Fund's limited resources by those borrowers which already have low residential rates? Is it really fair to the U.S. taxpayer who must subsidize these rates.

A related question which must be asked is "How should we divide the pie—the Revolving Fund?" S. 1300, upon close examination, actually treats all borrowers the same by requiring a minimum of 70 percent to be loaned from the Fund at the standard rate.

Residential consumers' rates differ a great deal from cooperative to cooperative. For example, while ten cooperatives had a typical residential electric bill greater than $120 for 1000 kwh, ten other cooperatives had a typical residential bill of less than $34 for the same amount of electricity. Is this really fair to consider all borrowers the same? Is it really fair to grant everyone a minimum 70 percent Federal share from the Fund's precious resources when the full 70 percent may not be necessary and thus could free up more money for other more needy borrowers? Is this also fair to those consumers who pay higher retail rates for their electricity from non-REA utilities?

The question of financial soundness also needs to be raised when we are dividing up the scarce resources of the Fund. There are two primary measures of financial soundness, TIER (Times Interest Earned Ratio) and equity. A TIER greater than 2.5 is generally considered adequate to be considered for private financing. The average IOU has a TIER of 2.3, yet is expected to receive all of its financing from the private sector. Surprisingly, testimony provided the Subcommittee indicates that there are more than 100 electric borrowers with a TIER greater than 5.0, yet all borrowers, regardless of the TIER ratio remain eligible for the subsidized standard rate for loans from the Fund. Is this fair to those cooperatives with very low TIER ratings?

The second measure of financial soundness is the level of equity, which also varies a great deal from cooperative to cooperative. An equity of 30 percent would generally be considered sufficient to obtain financing from private creditors. The average equity for IOU's is 40 percent and the mean value for cooperatives is 35 per-

cent. However, 50 cooperatives have an equity over 65 percent while, and at the same time, 50 cooperatives had an equity lower than 10 percent. Yet the higher equity cooperatives were required to be given the identical minimum financing level of 70 percent—the same minimum as the low equity borrowers. Is this fair to those low equity cooperatives? Is this really fair to most of those REA borrowers which are not yet sufficiently financially sound, to require that the minimum 70 percent be loaned from the Fund to those more financially sound cooperatives? Even the language of the 1973 Act which established the Fund encourages borrowers to "develop their resources and ability to satisfy their credit needs from their own financial organizations and other sources." The present language in S. 1300 precludes this move towards independence by restating the requirement that allows borrowers to receive at least 70 percent of their financing from the Revolving Fund. This further exhausts the assets of the Fund by allowing borrowers, who may not be in as great a need, full utilization of the Fund at the expense of their borrowing brothers. Is this fair? Shouldn't we consider methods to allow the Fund's scarce resources to be targeted to those who have greater needs as is the case in most other federal programs.

Another significant characteristic of some cooperatives was brought out during the Subcommittee hearings—that a large number of cooperatives sell more than 50 percent of their electricity to large industrial and commercial users. In fact, one cooperative sells only three percent of its service for residential use with most of its largest users being commercial mining companies. Other cooperatives also serve large industrial and commercial users such as aluminum companies, petroleum exploration and processing industries, pipeline and coal mining companies. In fact, 42 cooperatives sell over 50 percent of their electricity to these large businesses. Is it fair to treat all borrowers basically the same so that they receive a minimum of 70 percent of their financing needs from the Revolving Fund? It is fair to rural residential cooperatives which have nearly 100 percent of their consumers as residential users to be forced to compete with big businesses for the limited resources of the Fund?

While all borrowers are considered equal in that they all receive at least 70 percent of their financing from the Fund at standard rate loans, current law also recognizes that differences exist among cooperatives when determining eligibility for special rate loans. REA looks at potential special rate borrowers and considers them on their own merits to determine their eligibility. In addition, REA considers the characteristics of the individual borrowers when determining which cooperatives are to receive more than the minimum 70 percent federal financing. REA reviews potential recipient's characteristics in determining which should receive 70, 80, 90, or 100 percent of its financing needs through the Revolving Fund. And in some cases, due to unusual circumstances, REA will lend 100 percent of a borrower's needs at the special interest rate of 2 percent. While this examination of the characteristics of individual cooperatives is limited in scope, it does point out the inconsistency of guaranteeing every cooperative at least 70 percent of its financing regardless of its needs, while making distinctions in funding for

both 2 percent loans and for cooperatives which are to receive more than 70 percent minimum financing. Doesn't it appear more consistent to consider every borrower according to its own circumstances, in effect, targeting assistance to those rural Americans who need it the most.

What we should do in this legislation is create a structure wherein the resources of the Fund can be directed toward those borrowers who need greater assistance because of high rates, which might be caused by difficult terrain, high cost of power or other economic circumstances.

But instead of sharpening REA's ability to allocate scarce resources among the borrowers, I am left with the disquieting feeling that S. 1300 only further blurs those distinctions, locking in the same ratios, criteria, and loan program levels which contributed to the current Revolving Fund problems. The solution S. 1300 provides seems to make the taxpayer most responsible for saving the Fund. I am not convinced that solution is the correct one.

PAULA HAWKINS.

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ADDITIONAL VIEWS OF SENATOR RICHARD G. LUGAR

In the nearly 50 years of its existence, the Rural Electrification Administration has provided unquestioned benefits to all aspects of rural life. In 1935, when the REA was established, only 12 percent of our farms had electricity. Now, virtually all rural areas of the country are electrified, due in large measure to assistance provided by the Rural Electrification Administration.

Although REA's original mission to bring affordable electric service to rural America has been substantially achieved, the job is not complete. Many areas of the country, because of the high cost of power, low population density, rugged terrain, and other factors, still require assistance from the REA to maintain reliable and affordable electric and telephone service. This is an important objective and deserves the overwhelming support of Congress.

It is also clear, however, that some areas in need of this help in the 1930's no longer require it today. It is time to reevaluate the needs of the borrowers of the rural electric and telephone programs to ensure that only those rural residents who need the lower interest loans offered by REA continue to receive them. The REA borrowers who are now able, because of previous assistance, to obtain a greater share of their credit from non-Government sources should be required to do so.

The revolving fund

The Congress is addressing various proposals affecting the REA because the financing mechanism used to make loans to eligible borrowers is in danger of collapsing. In 1973, Congress established the Rural Electrification and Telephone Revolving Fund. All the outstanding indebtedness owed by REA borrowers on loans made from 1953 through 1973—approximately $7.9 billion—was placed in this fund as initial capital. The rate of interest on loans made to REA borrowers was fixed at 5 percent or, for hardship cases, 2 percent.

The revolving fund was established to operate on a self-sustaining basis. The revenue generated by repayments on laons previously made by REA was supposed to be adequate to meet its obligation and provide loans to electric and telephone borrowers. This self-sufficiency did not occur, however, and, in 1976, it was necessary for the REA to borrow additional funds from the U.S. Treasury to meet the annual level of lending mandated by Congress. This additional money was obtained from the Federal Financing Bank through documents called certificates of beneficial ownership in order to raise the additional funds needed to meet the congressionally mandated loan levels. Interest charges on all CBO's reflects the Government's cost of borrowing money.

The interest expense of this additional money borrowed annually by the revolving fund is not offset by an equal amount of interest

income flowing into the fund. This requires more CBO's to be sold which in turn obligates the fund for more interest charges. The growing expenses of the fund will eventually lead the revolving fund to insolvency. Table A shows the income and disbursements of the revolving fund since 1973. The interest payments made to the fund are insufficient to enable it to maintain self-sufficiency at the leading levels mandated by Congress.

Interest rates

A key factor in the fund's inability to become self-sufficient is the disparity between the interest income it receives and the interest expense it must pay. Congress, in the 1973 amendments to the Rural Electrification Act, established fixed rates of interest for loans made from the revolving fund. A rate of 5 percent was charged to all borrowers, except in hardship cases, when a 2-percent rate was charged. At the time these rates were established, the cost of money to the Government was 5.099 percent. It is clear that the substantial interest subsidies provided to REA borrowers were never intended by Congress, but rather that Congress intended to ensure that these borrowers had an adequate source of credit at rates comparable to those paid by the U.S. Treasury.

The interest rate charged REA borrowers had remained at 5 percent since 1973, even though the fund has paid interest rates as high as 15.325 percent on its CBO's. In 1983, the interest rate on funds borrowed by REA to meet mandated loan levels averaged 10.85 percent, while the interest income from REA loan repayments for the same year averaged only 4.90 percent. The fund was required to pay $367.9 million in interest payments that year on money it had previously borrowed. Table B shows the disparity in these interest rates each year since the program began in 1936.

It is clear that this wide gap between the interest rate charged to REA borrowers and the interest rate charged to the fund on its borrowing plays a primary role in the financial difficulty of the revolving fund. To alleviate this problem, Congress should provide a reasonable adjustment in the interest rates charged REA borrowers.

The interest rate formula in S. 1300, as amended by the Committee, may initially result in an interest rate charged to borrowers of between 6 and 6½ percent. Clearly this is not enough to provide the revenue the fund requires if it is to repay all its debts and remain solvent.

In fact, the inclusion of the provision in S. 1300 to forgive $7.9 billion in REA debt to the Treasury is necessary only because the bill neglects to set the interest rate at a level sufficient to enable the fund to repay the debt. The principal effect of this forgiveness is to give a greater interest rate subsidy to REA borrowers than would be the case if the fund was going to repay the $7.9 billion debt and still remain in balance. The large costs associated with this bill would be substantially reduced if the interest rate charged to borrowers was sufficient to generate revenues to repay the indebtedness of the fund. The Congressional Budget Office has estimated that S. 1300, as amended by the Committee, will increase Federal outlays by $9.3 billion from 1985 through 2010.

To the surprise of many, the interest rate necessary to provide for a solvent resolving fund and to repay all existing indebtedness would not cause substantial utility rate increases for rural electric and telephone consumers.

It is well-known that interest costs, in most cases, are a very small part of an REA electric or telephone consumer's bill. In fact, less than 5 percent of the monthly bill each consumer pays goes for interest expense. The "big ticket" electricity item that a consumer pays for is the cost of the power itself. This amounts, on average, to 70 percent of the rate charged. Estimates made by REA indicate that, for each 1 percent increase in the interest rate charged to REA borrowers, residential consumers' average monthly rates would increase by only ½ cent per day or 15 cents per month.

Most analyses indicate that an interest rate of 9 percent would be adequate to provide for the fund's solvency as well as enable it to repay all existing indebtedness, including the $7.9 billion debt to the Treasury due to be repaid in 1993. Therefore, an increase from the current interest rate of 5 percent to an interest rate of 9 percent would only cost consumers an average of 60 cents per month. This is certainly a nominal sum to pay in return for the future viability of the REA lending program. Of course, this 9-percent rate would still include a substantial subsidy for borrowers, since the interest rate for current long-term Treasury borrowing is about 13 percent.

During Committee markup, the Congressional Budget Office stated that interest rates to borrowers should eventually be lower under S. 2646, than under S. 1300. In fact, it is anticipated by the Congressional Budget Office that, under S. 1300, the interest rate will eventually equal or exceed the cost of money to the Government. Charts C and D, drawn from REA computer models, show that consumers would benefit more in the long run under the interest rate formula in S. 2646 when compared with the interest rate to be charged under S. 1300, as amended by the Committee.

The key factor in this analysis is that, if the current interest rate charged is adequate to make the fund self-sufficient, then future borrowing through the sale of CBO's will be eliminated. Thus, interest expense will be reduced. This, in turn, will enable the fund to charge its borrowers less and still maintain solvency.

The interest rate in S. 1300, as amended, will not be sufficient both to balance the fund and to allow it to repay its indebtedness. It is clear that the interest rate provided under S. 2646 will accomplish this necessary objective.

Supplemental financing ratios

Contributing to the pending insolvency of the revolving fund, in addition to interest rates, is the congressionally mandated lending level that requires a higher volume of loans than the fund can support on a self-sufficient basis.

Loan levels set by Congress each year have no relationship to the amount of income the fund receives from the repayment of previous loans. When the mandated lending levels exceed the revenue of the revolving fund, as they have every year since 1973, the fund must borrow additional money to make up the difference. This bor-

rowing, accomplished through the sale of CBO's to the Treasury, has occurred each year since 1976.

As the amount of this borrowing increases, the interest expense incurred by the fund increases. This expense siphons off fund resources that could otherwise go to making new electric and telephone loans.

S. 1300 does not address this most important issue. In fact, it encourages larger amounts of lending than the fund can support on a self-sustaining basis.

A provision in S. 1300 will require that 70 percent of each borrower's credit needs be met through subsidized loans from the revolving fund. No distinction is made between the wide differences in the capabilities of borrowers to obtain credit from non-Government sources. All borrowers are given the same level of subsidization, regardless of their level of need.

Any legislation to provide for a permanent solution to the revolving fund difficulties must seek to wean those borrowers from the revolving fund that no longer require this subsidized source of credit. In the 1930's, there was no doubt that most non-urban areas needed special help to obtain electricity and, in later years, telephone service. However, in the past half century our country has changed. Changes have also occurred in the financial circumstances of many of the borrowers who were deemed eligible for REA assistance in those early days. If a borrower initially served a "rural area", defined as a community with no more than 1,500 population, the borrower was eligible for REA assistance and remained so with no further review as to eligibility.

It is now obvious that Congress must reevaluate the mission of REA and direct the limited REA resources to those clearly in need of them.

The General Accounting Office testified before the Committee and provided the results of its survey of the financial status of electric cooperatives. In this survey, of the 922 electric distribution cooperatives in 1978, 386 (or 42 percent) had a times interest earned ratio of 2.5 or more and an equity ratio of 30 percent or more. These levels are generally regarded as sufficient to enable the cooperatives to obtain credit from the private market at reasonble rates and terms.

A factor that must be considered along with the financial well-being of the fund's borrowers is whether cooperatives served by the fund are essentially rural in nature. The Office of the Inspector General of the Department of Agriculture testified that a significant number of cooperatives are no longer "rural", yet they continue to receive financial assistance.

Also, there is concern that some cooperatives receiving REA assistance are not serving primarily rural residents, but rather large commercial and industrial customers. Table E contains examples of these types of cooperative.

Cooperatives serving nonrural areas and those that now have the financial capability of going to the private credit market for loan funds were never intended to receive the special assistance of the REA program. However, S. 1300 will not only continue to serve them, but will mandate that 70 percent of all these borrowers'

credit needs be supplied through the revolving funds. This is a serious handicap to the fund's becoming self-sufficient.

S. 1300 is flawed in that it contains no means test to identify borrowers in need of assistance so that an objective allocation can be made of the limited resources of the fund. With a lower volume of lending, the fund would need to borrow less additional money, thus substantially relieving the financial pressure on the fund.

Summation

It is clear that, through two basic adjustments to the REA program, the revolving fund can be made solvent and can provide a reliable, affordable source of credit to all rural borrowers truly in need of such assistance. These adjustments have not been made in S. 1300.

(1) Interest rates charged to REA borrowers must more closely reflect the interest rates paid by the Government for the money loaned. A subsidy should be provided to borrowers, but the spread between S. 1300 and the market rate is simply too large. This reduction in the subsidy can be accomplished, in most cases, with only minimal cost impact on rural consumers. The Congressional Budget Office estimates that an interest rate of approximately 9 percent—with some flexibility for fluctuating interest rates—would produce sufficient interest income to balance the fund.

(2) A means test should be instituted whereby those borrowers who are in less need of the assistance provided by REA reveive less of their credit needs ffom the revolving fund. As nonrural or financially secure cooperatives receive less REA assistance, the necessity for the revolving fund to borrow additional high cost capital will be reduced or eliminated altogether. This reduction in future interest expense will contribute substantially to the fund's solvency.

The REA has provided all Americans, not only those in rural areas, with immeasurable benefits during its relatively brief existence. The challenge to keep these programs both strong and fiscally responsible must be met so that people in all corners of this Nation can continue to obtain reliable and affordable electric and telephone service.

RICHARD G. LUGAR.

TABLE A.—THE RURAL ELECTRIFICATION AND TELEPHONE REVOLVING FUND (RETRF)

[In millions of dollars]

Fiscal year	Loan payments received		Retrf outlays	
	Principal	Interest	Advances to borrowers	Interest paid
1973	20.3	21.4	92.4	0
1974	173.1	144.2	802.4	0
1975	204.0	174.3	854.9	0
1976	299.2	252.3	1,027.9	11.4
1977	275.2	234.9	874.9	29.6
1978	303.1	268.1	881.4	33.3
1979	313.8	296.9	1,105.2	79.1
1980	349.1	336.9	1,206.8	144.1
1981	363.1	382.7	1,203.8	228.4

TABLE A.—THE RURAL ELECTRIFICATION AND TELEPHONE REVOLVING FUND (RETRF)—Continued

[In millions of dollars]

Fiscal year	Loan payments received		Retrf outlays	
	Principal	Interest	Advances to borrowers	Interest paid
1982	389.3	425.8	1,048.0	316.5
1983	405.2	459.1	855.6	367.9

TABLE B.—INTEREST RATE ON REA LOANS VS. COST OF MONEY TO THE GOVERNMENT

Fiscal year	REA loans [1]	Treasury issues [2]	Fiscal year	REA loans [1]	Treasury issues [2]
1936	3.00	2.530	1961	2.00	3.063
1937	2.77	2.525	1962	2.00	3.285
1938	2.88	2.521	1963	2.00	3.425
1939	2.73	2.525	1964	2.00	3.659
1940	2.69	2.492	1965	2.00	3.800
1941	2.46	2.413	1966	2.00	4.134
1942	2.48	2.225	1967	2.00	4.165
1943	2.57	1.822	1968	2.00	4.757
1944	2.67	1.725	1969	2.00	5.232
1945	2.00	1.718	1970	2.00	5.986
1946	2.00	1.773	1971	2.00	5.210
1947	2.00	1.871	1972	2.00	5.099
1948	2.00	1.942	1973	3.72	6.129
1949	2.00	2.001	1974	4.52	7.030
1950	2.00	1.958	1975	4.42	6.533
1951	2.00	1.981	1976	4.02	6.559
1952	2.00	2.051	TQ	3.92	6.591
1953	2.00	2.207	1977	3.88	6.481
1954	2.00	2.043	1978	4.35	7.388
1955	2.00	2.079	1979	4.27	8.592
1956	2.00	2.427	1980	4.37	9.608
1957	2.00	2.707	1981	4.38	12.435
1958	2.00	2.546	1982	4.48	12.082
1959	2.00	2.891	1983	4.90	10.850
1960	2.00	3.449			

[1] Weighted average interest rate on REA loans approved during the fiscal year paid by borrowers.
[2] Computed annual interest rate on marketable Treasury issues.

Source: Treasury Bulletin, U.S. Department of the Treasury.

TABLE C

STANDARD RATES UNDER S. 1300, AS AMENDED

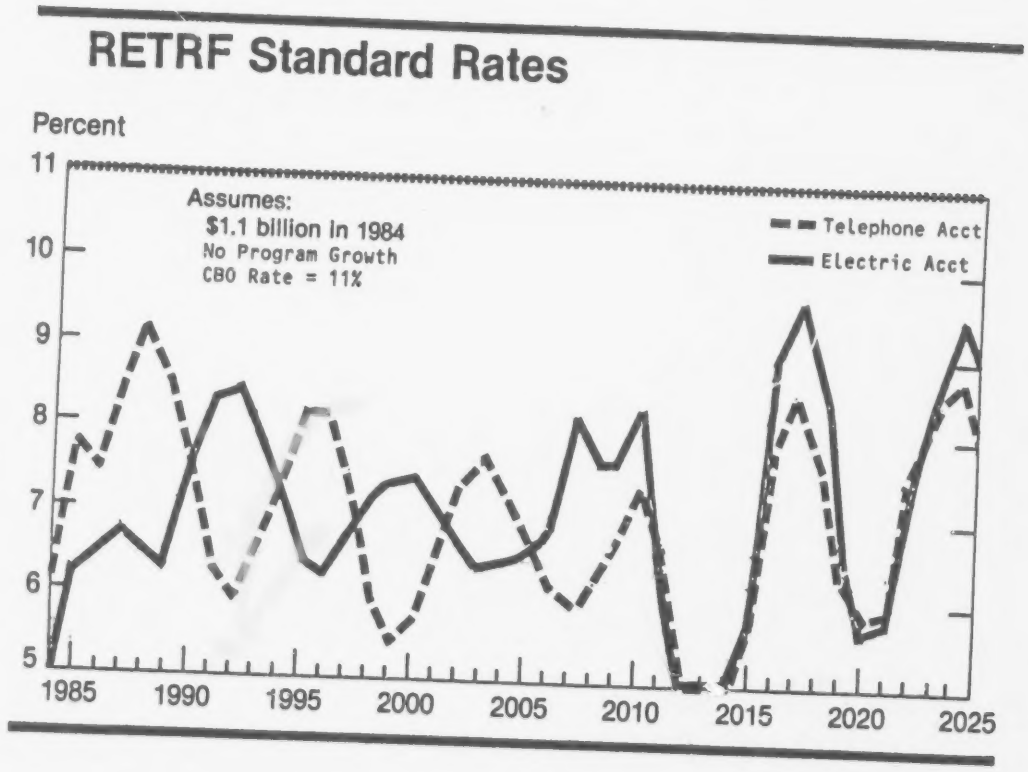

TABLE D

STANDARD RATES UNDER S. 2646

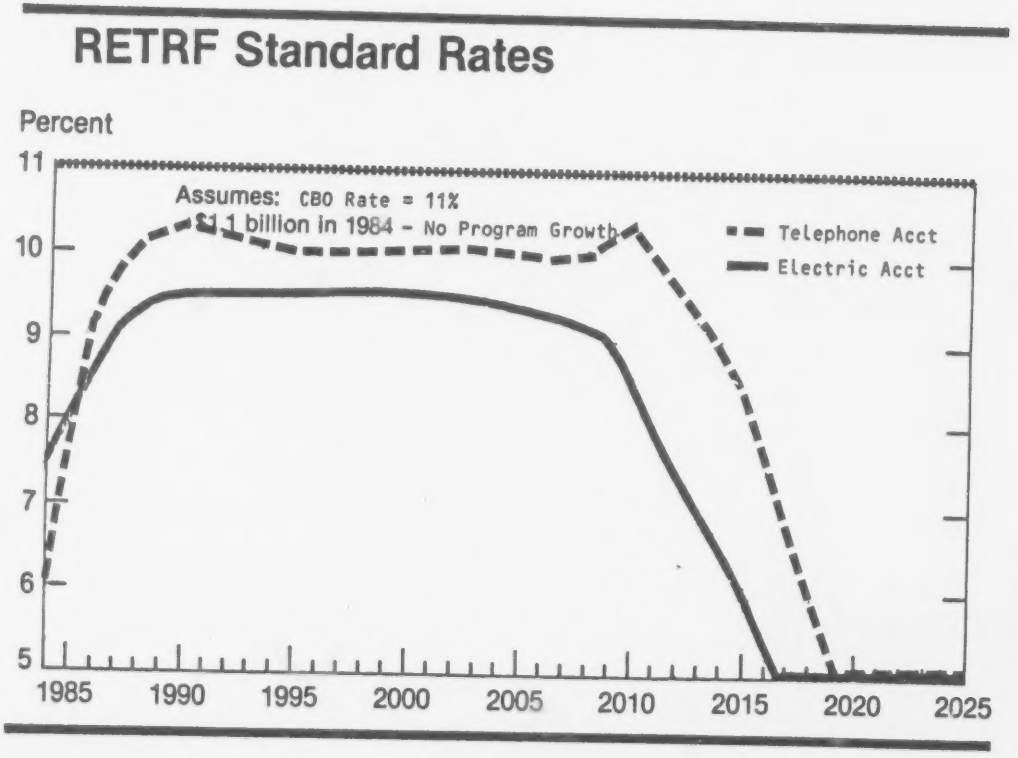

TABLE E.—EXAMPLES OF DISTRIBUTION BORROWERS WITH HIGH "LARGE COMMERCIAL AND INDUSTRIAL" SALES

Arizona 20: 88.8 percent of its sales (mWh) and 84.9 percent of its revenues are attributable to "large commercial and industrial" users. Indications are that most of those users are mining companies.

Arizona 23: 95.4 percent of its mWh sales and 94.3 percent of its revenues are from such consumers, most of whom appear to be involved in copper mining activities.

Kentucky 33: 91.5 percent of mWh sales and 86.3 percent of its revenues are attributable to such consumers, the largest of which appear to be aluminum companies.

Kentucky 55: 92.9 percent of mWh sales and 88 percent of revenues are tied to large commercial and industrial users, again primarily in the aluminum industry.

New Mexico 17: 75 percent of sales and 74.4 percent of revenues, primarily related to petroleum and pipeline industries.

New Mexico 22: 68.5 percent of mWh sales and 62.6 percent of revenues, for a variety of petroleum and mining consumers.

Utah 8: 83.6 percent of mWh sales and 79.5 percent of revenues, primarily for petroleum industry users.

Wyoming 3: 72.9 percent of mWh sales and 66.9 percent of revenues, primarily for petroleum industry consumers.

Wyoming 16: 91.7 percent of mWh sales and 90.7 percent of revenues, primarily for petroleum industry consumers.

Data based on CY 1982 sales statistics. National averages are: 24.4 percent of mWh sales for "large commercial and industrial"; 20.7 percent of revenues attributable to such consumers.

CHANGES IN EXISTING LAW

In compliance with paragraph 12 of rule XXVI of the Standing Rules of the Senate, changes in existing law made by the bill are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

RURAL ELECTRIFICATION ACT OF 1936

* * * * * * *

TITLE I

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That there is hereby created and established in the Department of Agriculture an agency of the United States, to be known as the "Rural Electrification Administration", all of the powers of which shall be exercised by an Administrator, under the general direction and supervision of the Secretary of Agriculture, who shall be appointed by the President, by and with the advice and consent of the Senate, for a

term of ten years. This Act may be cited as the "Rural Electrification Act of 1936".

SEC. 2. The Administrator is authorized and enpowered to make loans in the several States and Territories of the United States for rural electrification and the furnishing of electric energy to persons in rural areas who are not receiving central station service, and for the purpose of furnishing and improving telephone service in rural areas, as hereinafter provided; to make, or cause to be made, studies, investigations, and reports concerning the condition and progress of the electrification of and the furnishing of adequate telephone service in rural areas in the several States and Territories; and to publish and disseminate information with respect thereto.

SEC. 3. (a) The Secretary of the Treasury is hereby authorized and directed to make loans to the Administrator, upon the request and approval of the Secretary of Agriculture, in such amounts in the aggregate for each fiscal year commencing with the fiscal year ending June 30, 1948, as the Congress may from time to time determine to be necessary, either without interest or at such rate of interest per annum, not in excess of the rate provided for in sections 4 and 5 of this Act, as the Secretary of the Treasury may determine, upon the security of the obligations of borrowers from the Administrator appointed pursuant to the provisions of this Act or from the Administrator of the Rural Electrification Administration established by Executive Order Numbered 7037. Interest rates on the unpaid balance of any loans made by the Reconstruction Finance Corporation to the Administrator prior to July 1, 1947, shall be adjusted to the interest rate, if any, established for loans made after June 30, 1947, in accordance with the foregoing provisions: *Provided,* That such obligations incurred for the purpose of financing the construction and operation of generating plants, electric transmission and distribution lines, or systems and for the purpose of financing the improvement, expansion, construction, acquisition, and operation of facilities to render telephone service shall be fully amortized over a period not to exceed thirty-five years, and that the maturity of such obligations incurred for the purpose of financing the wiring of premises and the acquisition and installation of electrical and plumbing appliances and equipment shall not exceed two-thirds of the assured life thereof and not more than five years. The Administrator is hereby authorized to make all such endorsements, to execute all such instruments, and to do all such acts and things as shall be necessary to effect the valid transfer and assignment to the Secretary of the Treasury of all such obligations, and to execute such trust instruments as shall be agreed upon by the Administrator and the Secretary of the Treasury providing for the holding in trust by the Administrator of all such obligations for the Secretary of the Treasury as security for loans to the Administrator heretofore made by the Reconstruction Finance Corporation or made or to be made by the Secretary of the Treasury. All rights, interests, obligations, and duties of the Reconstruction Finance Corporation arising out of loans made or authorized to be made to the Administrator are, as of the close of June 30, 1947, vested in the Secretary of the Treasury; the Reconstruction Finance Corporation is authorized and directed to receive all loans outstanding on

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that date, plus accrued unpaid interest, theretofore made to the Administrator under the provisions of this Act, and all notes and other evidences thereof and all obligations constituting the security therefor. The Secretary of the Treasury shall cancel notes of the Reconstruction Finance Corporation, and sums due and unpaid upon or in connection with such notes at the time of such cancellation, in an amount equal to the unpaid principal of the loans so transferred, plus accrued unpaid interest through June 30, 1947. Subsequent to June 30, 1947, the Reconstruction Finance Corporation shall make no further loans or advances to the Administrator; and the Secretary of the Treasury is hereby authorized and directed, in lieu of the Reconstruction Finance Corporation, to lend or advance to the Administrator, in accordance with the provisions of this subsection 3(a), any unobligated or unadvanced balances of the sums which the Reconstruction Finance Corporation has theretofore been authorized and directed to lend to the Administrator. For the purpose of making loans or advances pursuant to this section, the Secretary of the Treasury is authorized to use as a public debt-transaction the proceeds from the sale of any securities issued under the Second Liberty Bond Act, as amended, and the purposes for which securities may be issued under that Act are extended to include such loans or advances to the Administrator. Repayments to the Secretary of the Treasury on such loans or advances shall be treated as a public-debt transaction of the United States.

(b) There are hereby authorized to be appropriated such sums as the Congress may from time to time determine to be necessary for the purposes of this Act as hereinafter provided.

(c) Twenty-five per centum of the annual sums herein made available or appropriated for loans for rural electrification pursuant to sections 4 and 5 of this title shall be allotted yearly by the Administrator for loans in the several States in the proportion which the number of their farms not then receiving central station electric service bears to the total number of farms of the United States not then receiving such service: *Provided,* That if any part of such sums are not loaned or obligated during the first six months of the fiscal year for which they are made available, such part shall thereafter be available for loans by the Administrator without allotment: *Provided, however,* That not more than 25 per centum of said sums may be employed in any one State or in all of the Territories. The Administrator shall within ninety days after the beginning of each fiscal year determine for each State and for the United States the number of farms not then receiving such service.

(d) The remaining 75 per centum of such annual sums shall be available for rural electrification loans in the several States and in the Territories, without allotment as hereinabove provided in such amounts for each State and Territory as, in the opinion of the Administrator, may be effectively employed for the purposes of this Act, and to carry out the provisions of section 7: *Provided, however,* That not more than 25 per centum of said unallotted annual sums may be employed in any one State, or in all of the Territories.

(e) If any part of the annual sums made available for the purposes of this Act are not loaned or obligated during the fiscal year for which they are made available, such unexpended or unobligated

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sums shall be available for loans by the Administrator in the following year or years without allotment: *Provided, however,* That not more than 25 per centum of said sums for rural electrification loans may be employed in any one State or in all of the Territories.

SEC. 4. The Administrator is authorized and empowered, from the sums hereinbefore authorized, to make loans for rural electrification to persons, corporations, States, Territories, and subdivisions and agencies thereof, municipalities, peoples' utility districts and cooperative, nonprofit, or limited dividend associations organized under the laws of any State or Territory of the United States, for the purpose of financing the construction and operation of generating plants, electric transmission and distribution lines or systems for the furnishing of electric energy to persons in rural areas who are not receiving central station service, and loans, from funds available under the provisions of section 3(b) and 3(e) but without regard to the 25 per centum limitation therein contained, to cooperative associations and municipalities for the purpose of enabling said cooperative associations and municipalities to the extent that such indebtedness was incurred with respect to electric transmission and distribution lines or systems or portions thereof serving persons in rural areas, to discharge or refinance long-term debts owed by them to the Tennessee Valley Authority on account of loans made or credit extended under the terms of the Tennessee Valley Authority Act of 1933, as amended: *Provided,* That the Administrator, in making such loans, shall give preference to States, Territories, and subdivisions and agencies thereof, municipalities, peoples' utility districts, and cooperative nonprofit, or limited dividend associations, the projects of which comply with the requirements of this Act. Such loans shall be on such terms and conditions relating to the expenditure of the moneys loaned and the security therefor as the Administrator shall determine and may be made payable in whole or in part out of the income: *Provided further,* That all such loans shall be selfliquidating within a period of not to exceed thirty-five years, and shall bear interest at the rate of 2 per centum per annum; interest rates on the unmatured and unpaid balance of any loans made pursuant to this section prior to September 21, 1944, shall be adjusted to 2 per centum per annum, and the maturity date of any such loans may be readjusted to occur at a date not beyond thirty-five years from the date of such loan: *And provided further,* That no loan for the construction, operation, or enlargement of any generating plant shall be made unless the consent of the State authority having jurisdiction in the premises is first obtained. Loans under this section and section 5 shall not be made unless the Administrator finds and certifies that in his judgment the security therefor is reasonably adequate and such loan will be repaid within the time agreed.

SEC. 5. The Administrator is authorized and empowered, from the sums hereinbefore authorized, to make loans for the purpose of financing the wiring of the premises of persons in rural areas and the aquisition and installation of electrical and plumbing appliances and equipment. Such loans may be made to any of the borrowers of funds loaned under the provisions of section 4, or to any person, firm, or corporation supply or installing the said wiring, appliances or equipment. Such loans shall be for such terms, subject

to such conditions, and so secured as reasonably to assure repayment thereof, and shall be at a rate of interest of 2 per centum per annum; interest rates on the unmatured and unpaid balance of any loans made pursuant to this section prior to September 21, 1944, shall be adjusted to 2 per centum per annum.

SEC. 6. For the purpose of administering this Act and for the purpose of making the studies, investigations, publications, and reports herein provided for, there is hereby authorized to be appropriated, out of any money in the Treasury not otherwise appropriated, such sums as shall be necessary. On or before February 15 of each calendar year beginning with calendar year 1976, or such other date as may be specified by the appropriate committee, the Secretary of Agriculture shall testify before the House Committee on Agriculture and the Senate Committee on Agriculture and Forestry and provide justification in detail of the amount requested in the budget to be appropriated for the next fiscal year for the purpose of administering this Act and for the purpose of making the studies, investigations, publications, and reports herein authorized.

SEC. 7. The Administrator is authorized and empowered to bid for and purchase at any foreclosure or other sale, or otherwise to acquire, property pledged or mortgaged to secure any loan made pursuant to this Act; to pay the purchase price and any costs and expenses incurred in connection therewith from the sums authorized in section 3 of this Act; to accept title to any property so purchased or acquired in the name of the United States of America; to operate or lease such property for such period as may be deemed necessary or advisable to protect the investment therein, but not to exceed five years after the acquisition thereof; and to sell such property so purchased or acquired, upon such terms and for such consideration as the Administrator shall determine to be reasonable.

No borrower of funds under section 4 or section 201 shall, without the approval of the Administrator, sell or dispose of its property, rights, or franchises, acquired under the provisions of this Act, until any loan obtained from the Rural Electrification Administration, including all interest and charges, shall have been repaid.

SEC. 8. The administration of loans and contracts entered into by the Rural Electrification Administration established by Executive Order Numbered 7037, dated May 11, 1935, may be vested by the President in the Administrator authorized to be appointed by this Act; and in such event the provisions of this Act shall apply to said loans and contracts to the extent that said provisions are not inconsistent therewith. The President may transfer to the Rural Electrification Administration created by this Act the jurisdiction and control of the records, property (including office equipment), and personnel used or employed in the exercise and performance of the functions of the Rural Electrification Administration established by such Executive Order.

SEC. 9. This Act shall be administered entirely on a nonpartisan basis, and in the appointment of officials, the selection of employees, and in the promotion of any such officials, or employees, no political test or qualification shall be permitted or given consideration, but all such appointments and promotions shall be given and made on the basis of merit and efficiency. If the Administrator

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herein provided for is found by the President of the United States to be guilty of a violation of this section, he shall be removed from office by the President, and any appointee or selection of officials or employees made by the Administrator who is found guilty of a violation of this Act shall be removed by the Administrator.

SEC. 10. The Administrator shall present annually to the Congress not later than the 20th day of April in each year a full report of his activities under this Act.

SEC. 11. In order to carry out the provisions of this Act the Administrator may accept and utilize such voluntary and uncompensated services of Federal, State, and local officers and employees as are available, and he may without regard to the provisions of civil-service laws applicable to officers and employees of the United States appoint and fix the compensation of attorneys, engineers, and experts, and he may, subject to the civil-service laws, appoint such other officers and employees as he may find necessary and prescribe their duties. The Administrator is authorized, from sums appropriated pursuant to section 6, to make such expenditures (including expenditures for personal services; supplies and equipment; lawbooks and books of reference, directories and periodicals; travel expenses; rental at the seat of government and elsewhere; the purchase, operation, or maintenance of passenger-carrying vehicles; and printing and binding) as are appropriate and necessary to carry out the provisions of this Act.

SEC. 12. The Administrator is authorized and empowered to extend the time of payment of interest or principal of any loans made by the Administrator pursuant to this Act: *Provided, however,* That with respect to any loan made under section 4 or section 201, the payment of interest or principal shall not be extended more than five years after such payment shall have become due, and with respect to any loan made under section 5, the payment of principal or interest shall not be extened more than two years after such payment shall have become due: *And provided further,* That the provisions of this section shall not apply to any obligations or the security therefor which may be held by the Reconstruction Finance Corporation under the provisions of section 3.

SEC. 13. As used in this Act the term "rural area" shall be deemed to mean any area of the United States not included within the boundaries of any city, village, or borough having a population in excess of fifteen hundred inhabitants, and such term shall be deemed to include both the farm and nonfarm population thereof; the term "farm" shall be deemed to mean a farm as defined in the publications of the Bureau of the Census; the term "person" shall be deemed to mean any natural person, firm, corporation, or association; the term "Territory" shall be deemed to include any insular possession of the United States.

SEC. 14. If any provision of this Act, or the application thereof to any person or circumstances, is held invalid, the remainder of the Act and the application of such provision to other persons or circumstances shall not be affected thereby.

SEC. 15. The Rural Electrification Administration is authorized to purchase such financial and credit reports as may be necessary to carry out its authorized work: *Provided,* That purchases under this authority shall not be made unless provision is made therefor in

the applicable appropriation and the cost thereof is not in excess of limitations prescribed therein.

SEC. 16. In order to insure coordination of electric generation and transmission financing under this Act with the national energy policy, the Administrator in making or guaranteeing loans for the construction, operations, or enlargement of generating plants or electric transmission lines or systems, shall consider such general criteria consistent with the provisions of this Act as may be published by the Secretary of Energy.

SEC. 17. The Administrator shall, upon application by a cooperative borrower located in a noncontiguous State not served by a statewide or multistate power grid, apply the same minimum financial standards, such as the "Times Interest Earned Ratio" (TIER), separately to the distribution assets and to the generation and transmission assets of such cooperative as are separately applied to a cooperative classified by the Administrator as being either a distribution cooperative or a generation and transmission cooperative.

TITLE II

SEC. 201. From such sums as are from time to time made available by the Congress to the Administrator for such purpose, pursuant to section 3 of this Act, the Administrator is authorized and empowered to make loans to persons now providing or who may hereafter provide telephone service in rural areas, to public bodies now providing telephone service in rural areas and to cooperative, nonprofit, limited dividend, or mutual associations. Except as otherwise provided by this title, such loans shall be made under the same terms and conditions as are provided in section 4 of this Act, for the purpose of financing the improvement, expansion, construction, acquisition, and operation of telephone lines, facilities or systems to furnish and improve telephone service in rural areas: *Provided, however,* That the Administrator, in making such loans shall give preference to persons providing telephone service in rural areas, to public bodies now providing telephone service in rural areas and to cooperative, nonprofit, limited dividend, or mutual associations: *And provided further,* That for a period of one year from and after the effective date of this title applications for loans received by the Administrator from persons who on the effective date of this title are engaged in the operation of existing telephone service in rural areas shall be considered and acted upon before action is taken upon any application received from any other person for any loan to finance the furnishing or improvement of telephone service to substantially the same subscribers. The Administrator in making such loans shall, insofar as possible, obtain assurance that the telephone service to be furnished or improved thereby will be made available to the widest practical number of rural users. When it is determined by the Administrator to be necessary in order to furnish or improve telephone service in rural areas, such loans may be made for the improvement, expansion, construction, acquisition, and operation of telephone lines, facilities, or systems without regard to their geographical location. The Administrator is further authorized and empowered to make loans for the purpose of refinancing outstanding indebtedness of persons furnishing tele-

phone service in rural areas: *Provided,* That such refinancing shall be determined by the Administrator to be necessary in order to furnish and improve telephone service in rural areas: *And provided further,* That such refinancing shall constitute not more than 40 per centum of any loan made under this title. [Loans under this section shall not be made unless the Administrator finds and certifies that in his judgment the security therefor is reasonably adequate and such loan will be repaid within the time agreed, nor shall such loan be made in any State which now has or may hereafter have a State regulatory body having authority to regulate telephone service and to require certificates of convenience and necessity to the applicant unless such certificate from such agency is first obtained. In a State in which there is no such agency or regulatory body legally authorized to issue such certificates to the applicant, no loan shall be made under this section unless the Administrator shall determine (and set forth his reasons therefor in writing) that no duplication of lines, facilities, or systems, providing reasonably adequate services will result therefrom.] *Loans under this section shall not be made unless the Administrator finds and certifies that, in the Administrator's judgment, the security therefor is reasonably adequate and such loans will be repaid within the time agreed.*

SEC. 202. Nothing contained in this Act shall be construed to deprive any State commission, board, or other agency of jurisdiction, under any State law, now or hereafter effective, to regulate telephone service which is not subject to regulation by the Federal Communications Commission, under the Communications Act of 1934, including the rates for such service.

[SEC. 203. (a) As used in this title, the term "telephone service" shall be deemed to mean any communication service for the transmission of voice, sounds, signals, pictures, writing, or signs of all kinds through the use of electricity between the transmitting and receiving apparatus, and shall include all telephone lines, facilities, or systems used in the rendition of such service; but shall not be deemed to mean message telegram service or community antenna television system services or facilities other than those intended exclusively for educational purposes, or radio broadcasting services or facilities within the meaning of section 3(o) of the Communications Act of 1934, as amended.

(b) As used in this title, the term "rural area" shall be deemed to mean any area of the United States not included within the boundaries of any incorporated or unincorporated city, village, or borough having a population in excess of one thousand five hundred inhibitants.]

SEC. 203. (a) As used in this title, the term "telephone service" shall be deemed to mean any communication service for the transmission of voice, sounds, signals, pictures, writing, or signs of all kinds by wire, fiber, radio, light, or other visual or electromagnetic means, and shall include all lines, facilities, or systems used in the rendition of such service, except that such term shall not be deemed to mean message telegram service or community antenna television system services or facilities other than those intended exclusively for educational purposes, or radio broadcasting services or facilities

within the meaning of section 3(o) of the Communications Act of 1934, as amended.

(b) As used in this title, the term "rural area" shall be deemed to mean any area of the United States not included within the boundaries of any incorporated or unincorporated city, village, or borough having a population in excess of two thousand five hundred inhabitants.

TITLE III

SEC. 301. RURAL ELECTRIFICATION AND TELEPHONE REVOLVING FUND.—(a) There is hereby established in the Treasury of the United States a fund, to be known as the Rural Electrification and Telephone Revolving Fund (hereinafter referred to as the "fund"), consisting of:

(1) all notes, bonds, obligations, liens, mortgages, and property delivered or assigned to the Administrator pursuant to loans heretofore or hereafter made under sections 4, 5, and 201 of this Act and under this title, as of the effective date of this title, as revised herein, and all proceeds from the sales hereunder of such notes, bonds, obligations, liens, mortgages, and property, which shall be transferred to and be assets of the fund;

(2) undisbursed balances of electric and telephone loans made under sections 4, 5, and 201, which as of the effective date of this title, as revised herein, shall be transferred to and be assets of the fund;

(3) notwithstanding section 3(a) of title I, all collections of principal and interest received on and after July 1, 1972, on notes, bonds, judgments, or other obligations made or held under titles I and II of this Act and under this title, except for net collection proceeds previously appropriated for the purchase of class A stock in the Rural Telephone Bank, which shall be paid into and be assets of the fund;

(4) all appropriations for interest subsidies and losses required under this title which may hereafter be made by the Congress and the unobligated balances of any funds made available for loans under the item "Rural Electrification Administration" in the Department of Agriculture and Agriculture-Environmental and Consumer Protection Appropriations Act;

(5) moneys borrowed from the Secretary of the Treasury pursuant to section 304(a); and

(6) shares of the capital stock of the Rural Telephone Bank purchased by the United States pursuant to section 406(a) of this Act and moneys received from said bank upon retirement of said shares of stock in accordance with the provisions of title IV of this Act, which said shares and moneys shall be assets of the fund.

SEC. 302. [LIABILITIES AND USES OF FUND.—(a) The notes of the Administrator to the Secretary of the Treasury to obtain funds for loans under sections 4, 5, and 201 of this Act, and all other liabilities against the appropriations or assets in the fund in connection with electrification and telephone loan operations shall be liabil-

ities of the fund, and all other obligations against such appropriations or assets in the fund arising out of electrification and telephone loan operations shall be obligations of the fund.] *EQUITY, LIABILITIES, AND USES OF THE FUND.—(a) The notes of the Administrator to the Secretary of the Treasury to obtain funds for loans under sections 4, 5, and 201 of this Act shall be equity capital of the fund. All liabilities against the appropriations or assets in the fund in connection with electrification and telephone loan operations shall be the fund, and all other obligations against such appropriations or assets in the fund arising out of electrification and telephone loan operations shall be obligations of the fund.*

(b) The assets of the fund shall be available only for the following purposes:

(1) loans which could be insured under this title, and for advances in connection with such loans and loans previously made, as of the effective date of this title, as revised herein, under sections 4, 5, and 201 of this Act;

[(2) payment of principal when due (without interest) on outstanding loans to the Administrator from the Secretary of the Treasury for electrification and telephone purposes pursuant to section 3(a) of this Act and payment of principal and interest when due on loans to the Administrator from the Secretary of the Treasury pursuant to section 304(a) of this title;]

(2) payment of principal and interest on loans to the Administrator from the Secretary of the Treasury under section 304(a) of this act and on certifictes of beneficial ownership issued to the Secretary of the Treasury or in the private market under section 304(c) of this act;

(3) payment of amounts to which the holder of notes is entitled on insured loans: *Provided,* That payments other than final payments need not be remitted to the holder until due or until the next agreed annual, semiannual, or quarterly remittance date;

(4) payment to the holder of insured notes of any defaulted installment or, upon assignment of the note to the Administrator at his request, the entire balance due on the note;

(5) purchase of notes in accordance with contracts of insurance entered into by the Administrator;

(6) payment in compliance with contracts of guarantee;

(7) payment of taxes, insurance, prior liens, expenses necessary to make fiscal adjustments in connection with the application, and transmittal of collections or necessary to obtain credit reports on applicants or borrowers, expenses for necessary services, including construction inspections, commercial appraisals, loan servicing, consultiong business advisory or other commercial and technical services and other program services, and other expenses and advances authorized in section 7 of this Act in connection with insured loans. Such items may be paid in connection with guaranteed loans after or in connection with the acquisition of such loans or security thereof after default, to the extent determined to be necessary to protect the interest of the Government, or in connection with any other activity authorized in this Act;

(8) payment of the purchase price and any costs and expenses incurred in connection with the purchase, acquisition, or operation of property pursuant to section 7 of this Act.

(c) The Administrator shall maintain two separate accounts within the fund, to be known as the Electrification Account and the Telephone Account, respectively. The assets, liabilities, income, expenses, and equity of the fund described in section 301 of this Act and subsection (a) of this section that are attributable to the operations of the electric loan program shall be accounted for in the Electrification Account, and the assets, liabilities, income, expenses, and equity of the fund so described that are attributable to the operations of the telephone loan program shall be accounted for in the Telephone Account. The assets accounted for in the Electrification Account shall be available only for the purposes described in subsection (b) of this section relating to the operations of the electric loan program, and the assets accounted for in the Telephone Account shall be available only for the purposes described in subsection (b) of this section relating to the operations of the telephone loan program.

SEC. 303. DEPOSIT OF FUND MONEYS.—Moneys in the fund shall remain on deposit in the Treasury of the United States until disbursed.

SEC. 304. FINANCIAL TRANSACTIONS OF THE FUND.—(a) The Administrator is authorized to make and issue interim notes to the Secretary of the Treasury for the purpose of obtaining funds necessary for discharging obligations of the fund and for making loans, advances and authorized expenditures out of the fund. Such notes shall be in such form and denominations and have such maturities and be subject to such terms and conditions as may be agreed upon by the Administrator and the Secretary of the Treasury. Such notes shall bear interest at a rate fixed by the Secretary of the Treasury, taking into consideration the current average market yield of outstanding marketable obligations of the United States having maturities comparable to the notes issued by the Administrator under this section. The Secretary of the Treasury is authorized and directed to purchase any notes of the Administrator issued hereunder, and, for that purpose, the Secretary of the Treasury is authorized to use as a public debt transaction the proceeds from the sale of any securities issued under the Second Liberty Bond Act, as amended, and the purposes for which such securities may be issued under such Act, as amended, are extended to include the purchase of notes issued by the Administrator. All redemptions, purchases, and sales by the Secretary of the Treasury of such notes shall be treated as public debt transactions of the United States:

Provided, however, That such interim notes to the Secretary of the Treasury shall not be included in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States.

(b) The Secretary of the Treasury is authorized and directed to purchase for resale obligations insured through the fund when offered by the Administrator. Such resales shall be upon such terms and conditions as the Secretary of the Treasury shall determine. Purchases and resales by the Secretary of the Treasury hereunder shall not be included in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States.

(c) The Administrator may, on an insured basis or otherwise, sell and assign any notes in the fund or sell certificates of beneficial ownership therein to the Secretary of the Treasury or in the private markets. Any sale by the Administrator of notes individually or in blocks shall be treated as a sale of assets for the purposes of the Budget and Accounting Act, 1921, notwithstanding the fact that the Administrator, under an agreement with the purchaser or purchasers, holds the debt instruments evidencing the loans and holds or reinvests payments thereon as trustee and custodian for the purchaser or purchasers of the individual note or of the certificate of beneficial ownership in a number of such notes. Security instruments taken by the Administrator in connection with any notes in the fund may constitute liens running to the United States notwithstanding the fact that such notes may be thereafter held by purchasers thereof. *Whenever the interest rate on any certificate of beneficial ownership that has a remaining term of seven years or more and that is issued by the Administrator and purchased under this subsection exceeds the rate of interest applicable to other similar certificate then being purchased by one hundred basis points (1 per centum) or more, the Administrator is authorized, after obtaining the prior approval of the President of the Federal Financing Bank, to repurchase the certificate. Such repurchase shall be made without penalty.*

SEC. 305. INSURED LOANS; INTEREST RATES AND LENDING LEVELS.—(a) The Administrator is authorized to make insured loans under this title and at the interest rates hereinafter provided to the full extent of the assets available in the fund, subject only to limitations as to amounts authorized for loans and advances as may be from time to time imposed by the Congress of the United States for loans to be made in any one year, which amounts shall remain available until expended: *Provided,* That the Congress in the annual appropriation Act may also authorize the transfer of any excess cash in the fund for deposit into the Treasury as miscellaneous receipts: *And provided further,* That any such loans and advances shall not be included in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States.

[(b) Insured loans made under this title shall bear interest at 5 per centum per annum, except that the Administrator may make

insured loans to electric or telephone borrowers at a lesser interest rate, but not less than 2 per centum per annum, if, in the Administrator's sole discretion, the Administrator finds that the borrower—

[(1) has experienced extreme financial hardships; or

[(2) cannot, in accordance with generally accepted management and accounting principles and without charging rates to its customers or subscribers so high as to create a substantial disparity between such rates and the rates charged for similar service in the same or nearby areas by other suppliers, provide service consistent with the objectives of this Act.]

(b) Insured loans made under this title from each account in the fund shall bear interest at a rate (hereinafter in this section referred to as the "standard rate") that shall be established by the Administrator and adjusted thereafter from time to time, under rules and regulations to be promulgated within one hundred and twenty days after the effective date of the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984. Such rules and regulations shall provide that the standard rate for each account shall be that rate, not less than 5 per centum per annum, that would produce, from loans (other than special rate loans) approved from that account during a given period, interest income equal to, but not greater than, the amount of anticipated interest expense on the account's obligations (interim notes, insured notes, and certificates of beneficial ownership) required to be issued or sold during such period to cover loan advances and interest expenses: Provided, That the amount of such obligations to be issued or sold for such purposes shall be determined by deducting the sum of principal and interest receipts and any appropriation under subsection (c) of this section from the sum of loan advances and interest expenses on outstanding obligations of the account during such period: Provided further, That the standard rate determined by the Administrator for each account shall be sufficient to produce total anticipated interest income (including any appropriated funds and interest income from outstanding loans) for such account that will be equal to the total anticipated interest expense on all outstanding obligations of that account. The standard rate and any adjustment thereto shall be established or made having due regard for the objectives of this Act and shall be applicable only to loans made after the effective date of such establishment or adjustment. The Administrator shall make insured loans to electric or telephone borrowers at a lesser rate of interest, but not less than 2 per centum per annum nor more than a rate equal to one-half the standard rate (referred to in this section as the "special rate"), if the Administrator finds, under guidelines to be established within one hundred and twenty days after the effective date of the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984, that the borrower—

(1)(A) charges rates exceeding twice the national average of rates charged by borrowers in the same program, or cannot provide service consistent with the objectives of this Act without charging rates (established in accordance with generally accepted management and accounting principles) so high as to create a substantial disparity between such rates and the rates

charged for similar service in the same or nearby areas by other suppliers; or

(B) has an average consumer density of two or fewer per mile of line; or

(C) has experienced financial losses attributable to storm damage, natural disasters, or other occurrences beyond its control; or

(D) serves geographic areas having unusually low per capita income; and

(2) is experiencing financial hardship as determined by investment in utility plant in service per consumer served being at least twice the national average of other borrowers in the same program or other financial or other hardship, through extenuating circumstances, as determined by the Administrator.

The rules and regulations promulgated under this subsection shall not take effect until (1) such rules and regulations have been transmitted to the Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture and (2) the expiration of thirty calendar days of continuous session of Congress after the date of such transmittal.

(c)(1) The Administrator shall establish in the Electrification Account and in the Telephone Account a reserve to be used to cover the cost to each account of loans made at the special rate. At the beginning of each fiscal year, the Administrator shall place in each reserve an amount equal to 1 per centum of the payments of principal and interest into the account during the preceding fiscal year. The Administrator shall apply the funds in each reserve against the estimated total cost to each account, through the period ending with the review required by paragraph (2), of all electric and telephone loans, respectively, that are made or extended at the special rate under this section during the fiscal year. If the Administrator determines that, as of the end of the fiscal year, either reserve is not adequate to cover fully such cost, the Administrator shall promptly so notify the Secretary of Agriculture, who shall include in the Secretary's next supplemental budget estimate or request submitted to the President or the Office of Management and Budget, and shall concurrently submit to the House Committee on Appropriations, the House Committee on Agriculture, the Senate Committee on Appropriations, and the Senate Committee on Agriculture, Nutrition, and Forestry, a request for funds necessary to cover the balance of such cost.

(2) Each loan made at the special rate shall be reviewed by the Administrator every five years to determine whether the borrower continues to qualify for the special rate loan under the criteria specified in subsection (b) of this section. The Administrator shall (A) extend the loan at the special rate for an additional five-year period if the borrower is determined to continue to qualify, or (B) adjust the interest rate on the loan to the then current standard rate if the borrower is determined no longer to qualify.

[(c)] *(d)* Loans made under this section shall be insured by the Administrator when purchased by a lender. As used in this Act, an insured loan is one which is made, held, and serviced by the Administrator, and sold and insured by the Administrator hereiunder

[; such loans shall be sold and insured by the Administrator without undue delay].

SEC. 306. GUARANTEED LOANS; ACCOMMODATION AND SUBORDINATION OF LIENS.—[The Administrator may provide financial assistance to borrowers for purposes provided in the Rural Electrification Act of 1936, as amended, by guaranteeing loans, in the full amount thereof, made by the Rural Telephone Bank, National Rural Utilities Cooperative Finance Corporation, and any other legally organized lending agency, or by accommodating or subordinating liens or mortgages in the fund held by the Administrator as owner or as trustee or custodian for purchases of notes from the fund, or by any combination of such guarantee, accommodation, or subordination.] *(a) For the purposes of (1) encouraging and assisting borrowers to develop and achieve the financial strength necessary to satisfy their credit needs from other sources and (2) improving the financial stability of borrowers, the Administrator, consistent with the objectives of this Act and in accordance with the rules and regulations to be promulgated under subsection (b) of this section, shall provide financial assistance to borrowers for purposes provided in this Act and for purposes of providing refinancing assistance, by guaranteeing loans, in the full amount thereof, made by the Rural Telephone Bank, the National Rural Utilities Cooperative Finance Corporation, or any other legally organized lending agency or lender approved by the Administrator, or by accommodating or subordinating liens or mortgages in the fund held by the Administrator as owner or as trustee or custodian for purchases of notes from the fund, or by any combination of such guarantee, accommodation, or subordination. The Administrator shall accommodate or subordinate liens or mortgages at the request of the borrower, notwithstanding any other provision of this Act, for any purpose that would enhance the financial strength or revenue of the borrower or improve the efficiency, effectiveness, or financial stability of the borrower, upon a finding that the borrower has, or will have, the ability to repay its existing and proposed indebtedness.* No fees or charges shall be assessed for any such guarantee, accommodation, or subordination. With respect to guarantees issued by the Administrator under this section, on the request of the borrower of any such loan so guaranteed, the loan shall be made by the Federal Financing Bank and at a rate of interest that is not more than the rate of interest applicable to other similar loans then being made or purchased by the Bank. Guaranteed loans shall bear interest at the rate agreed upon by the borrower and the lender. Guaranteed loans, and accommodation and subordination of liens or mortgages, may be made concurrently with an insured loan. the amount of guaranteed loans shall be subject only to such limitations as to amounts as may be authorized from time to time by the Congress of the United States: *Provided*, that any amounts guaranteed hereunder shall not be included in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States. [As used in this title, a guaranteed loan is one which is initially made, held, and serviced by a legally organized lending agency and which is guaranteed by the Administrator hereunder.] *As used in this title, the term "guaran-*

teed loan" means a loan that is initially made or refinanced, held, and serviced by a legally organized lending agency or lender approved by the Administrator and that is guaranteed by the Administrator hereunder. A guaranteed loan, including the related guarantee, may be assigned to the extent provided in the contract of guarantee executed by the Administrator under this title; the assignability of such loan and guarantee shall be governed exclusively by said contract of guarantee.

(b) Not later than ninety days after the effective date of the Rural Electrification and Telephone Revolving Fund Self-Sufficiency Act of 1984, the Administrator shall promulgate rules and regulations for the guarantee of loans and the accommodation and subordination of liens or mortgages, as provided in subsection (a) of this section. The rules and regulations promulgated under this subsection shall not take effect until (1) such rules and regulations have been transmitted to the Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture and (2) the expiration of thirty calendar days of continuous session of Congress after the date of such transmittal.

(c) Whenever the interest rate on any advance under a loan that has a remaining term of seven years or more and that is guaranteed by the Administrator and made by a lender under this section exceeds the rate of interest applicable on other similar new advances then being made or purchased by one hundred basis points (1 per centum) or more, the lender is authorized, upon the request of the borrower, to adjust the interest rate on such advance, without penalty, to the interest rate than applicable to other similar new advances then being made or purchased by the lender: Provided, That no interest rate on such advance shall be readjusted at intervals of less than seven years.

SEC. 307. OTHER FINANCING.—When it appears to the Administrator that the loan applicant is able to obtain a loan for part of his credit needs from a responsible cooperative or other credit source at reasonable rates and terms consistent with the loan applicant's ability to pay and the achievement of the Act's objectives, he may request the loan applicant to apply for and accept such a loan concurrently with an insured loan, subject, however, to full use being made by the Administrator of the funds made available hereunder for such insured loans under this title: *Provided, That in any fiscal year for which the minimum loan level, as established by law, is less than $1,000,000,000 for insured loans for rural electrification, rural electrification borrowers shall obtain concurrent supplemental financing in accordance with the applicable criteria and ratios in effect for fiscal year 1983 under Public Law 97-370, 96 Stat. 1801, enacted December 18, 1982.*

SEC. 308. FULL FAITH AND CREDIT OF THE UNITED STATES.—Any contract of insurance or guarantee executed by the Administrator under this title shall be an obligation supported by the full faith and credit of the United States and incontestable except for fraud or misrepresentation of which the holder had actual knowledge at the time it became a holder.

SEC. 309. LOAN TERMS AND CONDITIONS.—Loans made from or insured through the funds shall be for the same purposes and on the same terms and conditions as are provided for loans in titles I and

II of this Act except as otherwise provided in sections 303 to 308 inclusive.

SEC. 310. REFINANCING OF RURAL DEVELOPMENT ACT LOANS.—At the request of the borrower, the Administrator is authorized and directed to refinance with loans which will be insured under this Act, at the interest rates provided in section 305, any loans made for rural electric and telephone facilities under any provision of the Consolidated Farm and Rural Development Act.

TITLE IV

SEC. 401. ESTABLISHMENT, GENERAL PURPOSES, AND STATUS OF THE TELEPHONE BANK.—(a) There is hereby established a body corporate to be known as the Rural Telephone Bank (hereinafter called the telephone bank).

(b) The general purposes of the telephone bank shall be to obtain an adequate supply of supplemental funds to be extent feasible from non-Federal sources, to utilize said funds in the making of loans under section 408 of this title, and to conduct its operations to the extent practicable on a self-sustaining basis.

(c) The telephone bank shall be deemed to be an instrumentality of the United States, and shall, for the purposes of jurisdiction and venue, be deemed a citizen and resident of the District of Columbia. The telephone bank is authorized to make payments to State, territorial, and local governments in lieu of property taxes upon real property and tangible personal property which was subject to State, territorial, and local taxation before acquisition by the telephone bank. Such payment may be in the amounts, at the times, and upon such terms as the telephone bank deems appropriate but the telephone bank shall be guided by the policy of making payments not in excess of the taxes which would have been payable upon such property in the condition in which it was acquired.

SEC. 402. GENERAL POWERS.—To carry out the specific powers herein authorized, the telephone bank shall have power to (a) adopt, alter, and use a corporate seal; (b) sue and be sued in its corporate name; (c) make contracts, leases, and cooperative agreements, or enter into other transactions as may be necessary in the conduct of its business, and on such terms as it may deem appropriate; (d) acquire, in any lawful manner, hold, maintain, use, and dispose of property: *Provided*, That the telephone bank may only acquire property needed in the conduct of its banking operations or pledged or mortgaged to secure loans made hereunder or in temporary operation or maintenance thereof: *Provided further*, That any such pledged or mortgaged property so acquired shall be disposed of as promptly as is consistent with prudent liquidation practices, but in no event later than five years after such acquisition; (e) accept gifts or donations of services or of property in aid of any of the purposes herein authorized; (f) appoint such officers, attorneys, agents, and employees, vest them with such powers and duties, fix and pay such compensation to them for their services as the telephone bank may determine; (g) determine the character of and necessity for its obligations and expenditures, and the manner in which they shall be incurred, allowed, and paid; (h) execute, in accordance with its bylaws, all instruments necessary or appropriate

in the exercise of any of its powers; (i) collect or compromise all obligations assigned to or held by it and all legal or equitable rights accruing to it in connection with the payment of such obligations until such time as such obligations may be referred to the Attorney General for suit or collection; and (j) exercise all such other powers as shall be necessary or incidental to carrying out its functions under this title.

SEC. 403 SPECIAL PROVISIONS GOVERNING TELEPHONE BANK AS AN AGENCY OF THE UNITED STATES UNTIL CONVERSION OF OWNERSHIP, CONTROL, AND OPERATION.—Until the ownership, control, and operation of the telephone bank is converted as provided in section 410(a) of this title and not thereafter:

(a) The telephone bank shall be an agency of the United States and shall be subject to the supervision and direction of the Secretary of Agriculture (hereinafter called the Secretary): *Provided, however,* That the telephone bank shall at not time be entitled to transmission of its mail free or postage, nor shall it have the priority of the United States in the payment of debts out of bankrupt, insolvent, and decedents' estates.

(b) In order to perform its responsiblities under this title, the telephone bank may partially or jointly utilize the facilities and the services of employees of the Rural Electrification Adminstration or of any other agency of the Department of Agriculture, without cost to the telephone bank.

(c) The telephone bank shall be subject to the provisions of the Government Corporation Control Act, as amended (31 U.S.C. 841, et seq.), in the same manner and to the same extent as if it were included in the definition of "wholly owned Government corporation" as set forth in section 101 of said Act (31 U.S.C. 846).

(d) The telephone bank may withoiut regard to the civil service classification laws appoint and fix the compensation of such officers and employees of the telephone bank as it may deem necessary.

(e) The telephone bank shall be subject to the provisions of sections 517, 519, and 2679 of title 28, United States Code.

SEC. 404. GOVERNOR.—Subject to the provisions of section 410, the Administrator of the Rural Electrification Administration shall serve as the chief executive officer of the telephone bank (herein called the Governor of the telephone bank). Except as to matters specifically reserved to the Telephone Bank Board in this title, the Governor of the telephone bank shall exercise and perform all functions, powers, and duties of the telephone bank.

SEC. 405. BOARD OF DIRECTORS.—(a) The management of the telephone bank, within the limitations prescribed by law, shall be vested in a board of directors (herein called the Telephone Bank Board) consisting of thirteen members.

(b) The Administrator of the Rural Electrification Administration and the Governor of the Farm Credit Administration shall be members of the Telephone Bank Board. Five other members of the Telephone Bank Board shall be designated by the President to serve at his pleasure, three of whom shall be officers or employees of the Department of Agriculture but not officers or employees of the Rural Electrification Administration, and two of whom shall be from the general public and not officers or employees of the Feder-

al Government. The Administrator and other officers and employees of the Department of Agriculture and the Governor of the Farm Credit Administration shall serve as members without additional compensation.

(c) As soon as practicable after enactment of this title, the President of the United States shall appoint six additional members of the initial Telephone Bank Board to be selected from the directors, managers, and employees of any entities eligible to borrow from the telephone bank and of organizations controlled by such entities, with due regard to fair representation of the rural telephone systems of the Nation. The six members thus appointed shall serve until their successors shall have been duly elected in accordance with subsection (d).

(d) Within twelve months following the appointment of the six members of the initial Board as provided in subsection (c), the Governor of the telephone bank shall call a meeting of all entities then eligible to borrow from the telephone bank and organizations controlled by such entities for the purpose of electing members of the Telephone Bank Board. Each such entity and organization shall be entitled to notice of and shall have one noncumulative vote at said meeting. Six members of the Telephone Bank Board shall be elected for a two-year term, three from among the directors, managers, and employees of cooperative-type entities eligible to vote and organizations controlled by such entities, and three from among the managers, directors, and employees of commercial-type entities eligible to vote and organizations controlled by such entities. These six members shall be elected by majority vote of the entities and organizations eligible to vote and such entities and organizations may vote by proxy.

(e) Thereafter, the cooperative-type entities and organizations holding class B and class C stock, voting as a separate class, shall elect three directors to represent their class by a majority vote of the stockholders voting in such class; and the commercial-type entities and organizations holding class B and class C stock, voting as a separate class, shall elect three directors to represent their class by a majority vote of the stockholders voting in such class. Limited proxy voting may be permitted, as authorized by the bylaws of the telephone bank. Cumulative voting shall not be permitted.

(f) Any Telephone Bank Board member may continue to serve after the expiration of the term for which he is elected until his successor has been elected and has qualified. Telephone Bank Board members designated from the general public, pursuant to subsection (b), or appointed or elected pursuant to subsections (c), (d), and (e), shall receive $100 for each day or part thereof, not to exceed one hundred days per year for the first three years after enactment of this title and not to exceed fifty days per year thereafter, spent in the performance of official duties, and shall be reimbursed for travel and other expenses in such manner and subject to such limitations as the Telephone Bank Board may prescribe.

(g) The Telephone Bank Board shall prescribe bylaws, not inconsistent with law, regulating the manner in which the telephone bank's business shall be conducted, its directors and officers elected, its stock issued, held, and disposed of, its property transferred,

its bylaws amended, and the powers and privileges granted to it by law exercised and enjoyed.

(h) The Telephone Bank Board shall meet at such times and places as it may fix and determine, but shall hold at least four regularly scheduled meetings a year, and special meetings may be held on call in the manner specified in the bylaws of the telephone bank.

(i) The Telephone Bank Board shall make an annual report to the Secretary for transmittal to the Congress on the administration of this title IV and any other matters relating to the effectuation of the policies of title IV, including recommendations for legislation.

SEC. 406. CAPITALIZATION.—The telephone bank's capital shall consist of capital subscribed by the United States, by borrowers from the telephone bank, by corporations and public bodies eligible to become borrowers from the telephone bank, and by organizations controlled by such borrowers, corporations, and public bodies. Beginning with the fiscal year 1971 and for each fiscal year thereafter [but not later than fiscal year 1991], the United States shall furnish capital for the purchase of class A stock and there are hereby authorized to be appropriated such amounts, not to exceed $30,000,000 annually, for such purchases until such class A stock shall equal $600,000,000, *Provided,* That on or before July 1, 1975, the Secretary shall make a report to the President for transmittal to the Congress on the status of capitalization of the telephone bank by the United States with appropriate recommendations. As used in this section and section 301, the term "net collection proceeds" shall be deemed to mean payments from and after July 1, 1969, of principal and interest on loans heretofore or hereafter made under section 201 of this Act, less an amount representing interest payable to the Secretary of the Treasury on loans to the Administrator for telephone purposes pursuant to section 3(a) of this Act.

(b) The capital stock of the telephone bank shall consist of three classes, class A, class B, and class C, the rights, powers, privileges, and preferences of the separate classes to be as specified, not inconsistent with law, in the bylaws of the telephone bank. Class B and class C stock shall be voting stock, but no holder of said stock shall be entitled to more than one vote, nor shall class B and class C stockholders, regardless of their number, which are owned or controlled by the same person, group of persons, firm, association, or corporation, be entitled in any event to more than one vote.

(c) Class A stock shall be issued only to the Administrator of the Rural Electrification Administration on behalf of the United States in exchange for capital furnished to the telephone bank pursuant to subsection (a), and such class A stock shall be redeemed and retired by the telephone bank as soon as practicable after September 30, 1995, but not to the extent that the Telephone Bank Board determines that such retirement will impair the operations of the telephone bank: *Provided,* That the minimum amount of class A stock that shall be retired each year after said date shall equal the amount of class B stock sold by the telephone bank during such year. Class A stock shall be entitled to a return, payable from income, at the rate of 2 per centum per annum on the amounts of said class A stock actually paid into the telephone bank. Such

return shall be cumulative and shall be payable annually into miscellaneous receipts of the Treasury.

(d) Class B stock shall be held only by recipients of loans under section 408 of this Act. Borrowers receiving loan funds pursuant to section 408(a) (1) or (2) shall be required to invest in class B stock 5 per centum of the amount of loan funds so provided. No dividends shall be payable on class B stock. All holders of class B stock shall be entitled to patronage refunds in class B stock under terms and conditions to be specified in the bylaws of the telephone bank.

(e) Class C stock shall be available for purchase and shall be held only by borrowers, or by corporations and public bodies eligible to borrow under section 408 of this Act, or by organizations controlled by such borrowers, corporations and public bodies, and shall be entitled to dividends in the manner specified in the bylaws of the telephone banks. Such dividends shall be payable only from income and, until all class A stock is retired, shall not exceed the current average rate payable on its telephone debentures.

(f) If a firm, association, corporation, or public body is not authorized under the laws of the jurisdiction in which it is organized to acquire stock of the telephone bank, the telephone bank shall, in lieu thereof, permit such organization to pay into a special fund of the telephone bank a sum equivalent to the amount of stock to be purchased. Each reference in this title to capital stock, or to class B or class C stock, shall include also the special fund equivalents of such stock, and to the extent permitted under the laws of the jurisdiction in which such organization is organized, a holder of special fund equivalents of class B, or class C stock, shall have the same rights and status as a holder of class B, or class C stock, respectively. The rights and obligations of the telephone bank in respect of such special fund equivalent shall be identical to its rights and obligations in respect of class B, or class C stock, respectively.

(g) After payment of all operating expenses of the telephone bank, including interest on its telephone debentures, setting aside appropriate funds for reserves for losses, and making payment in lieu of taxes, and returns on Class A stock as provided in section 406(c), and on Class C Stock, the Telephone Bank Board shall annually set aside the remaining earnings of the telephone bank for patronage refunds in accordance with the bylaws of the telephone bank.[

SEC. 407. BORROWING POWER.—(a) The telephone bank is authorized to obtain funds through the public or private sale of its bonds, debentures, notes, and other evidences of indebtedness (herein collectively called telephone debentures). Telephone debentures shall be issued at such times, bear interest at such rates, and contain such other terms and conditions as the Telephone Bank Board shall determine: *Provided, however,* That the amount of the telephone debentures which may be outstanding at any one time pursuant to this section shall not exceed twenty times the paid-in capital and retained earnings of the telephone bank. Telephone debentures shall not be exempt, either as to principal or interest, from any taxation now or hereafter imposed by the United States, by any territory, dependency, or possession, thereof, or by any State or local taxing authority. Telephone debentures shall be lawful investments and may be accepted as security for all fiduciary, trust, and

public funds, the investment or deposit of which shall be under the authority and control of the United States or any officer or officers thereof.

(b) The Telephone Bank is also authorized to issue telephone debentures to the Secretary of the Treasury, and the Secretary of the Treasury may in his discretion purchase any such debentures, and for such purpose the Secretary of the Treasury is authorized to use as a public debt transaction the proceeds of the sale of any securities hereafter issued under the Second Liberty Bond Act, as now or hereafter in force, and the purposes for which securities may be issued under the Second Liberty Bond Act as now or hereafter in force are extended to include such purchases. Each purchase of telephone debentures by the Secretary of the Treasury under this subsection shall be upon such terms and conditions as to yield a return at a rate not less than a rate determined by the Secretary of the Treasury, taking into consideration the current average yield on outstanding marketable obligations of the United States of comparable maturity. The Secretary of the Treasury may sell, upon such terms and conditions and at such price or prices as he shall determine, any of the telephone debentures acquired by him under this subsection. All purchases and sales by the Secretary of the Treasury of such debentures under this subsection shall be treated as public debt transactions of the United States.

(c) Purchases and resales by the Secretary of the Treasury as authorized in subsection (b) of this section shall not be included in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States.

SEC. 408. LENDING POWER.—(a) The Governor of the telephone bank is authorized on behalf of the telephone bank to make loans, in conformance with policies approved by the Telephone Bank Board, to corporations and public bodies which have received a loan or loan commitment pursuant to section 201 of this Act, or which have been certified by the Administrator to be eligible for such a loan or loan commitment, (1) for the same purposes and under the same limitations for which loans may be made under section 201 of this Act (2) for the purposes of financing, or refinancing, the construction, improvement, expansion, acquisition, and operation of telephone lines, facilities, or systems, in order to improve the efficiency, effectiveness, or financial stability of borrowers financed under sections 201 and 408 of this Act, and (3) for the purchase of class B stock required to be purchased under Section 406(d) of this Act but not for the purchase of class C stock [, subject, as to the purposes set forth in (2) hereof, to the following provisos: That in the case of any such loan for the acquisition of telephone lines, facilities, or systems, the acquisition shall be approved by the Secretary, the location and character thereof shall be such as to improve the efficiency, effectiveness, or financial stability of the telephone system of the borrower, and in respect of exchange facilities for local services, the size of each acquisition shall not be greater than the borrower's existing system at the time it receives its first loan from the telephone bank, taking into account the number of subscribers served, miles of line, and plant investment]. Loans and advances made under this section shall not be included

in the totals of the budget of the United States Government and shall be exempt from any general limitation imposed by statute on expenditures and net lending (budget outlays) of the United States.

(b) Loans under this section shall be on such terms and conditions as the Governor of the telephone bank shall determine, subject, however, to the following restrictions:

(1) All loans made under this section shall be fully amortized over a period not to exceed fifty years.

(2) Funds to be loaned under this Act to any borrower shall be loaned under this section in preference to section 201 if the borrower is eligible for such a loan and funds are available therefor. Notwithstanding the foregoing or any other provision of law, all loans made pursuant to this Act for facilities for telephone systems with an average subscriber density of three or fewer per mile shall be made under section 201 of this Act: but this provision shall not preclude the making of such loans from the telephone bank at the election of the borrower.

(3) Loans under this section shall bear interest at the "cost of money rate." The cost of money rate is defined as the average cost of moneys to the telephone bank as determined by the Governor, but not less than 5 per centum per annum.

(4) Loans shall not be made under this section unless the Governor of the telephone bank finds and certifies that in his judgment (i) the security therefor is reasonably adequate and such loan will be repaid within the time agreed, and (ii) the borrower has the capability of producing net income or margins before interest *and income taxes* at least equal to 150 per centum of the interest requirements on all of its outstanding and proposed loans, or such [higher] *other* per centum as may be fixed from time to time by the Telephone Bank Board in order to allocate available funds equitably among borrowers or to improve the marketability of the telephone debentures: *Provided, however,* That the Governor of the telephone bank may waive the requirement of (ii) above in any case if he shall determine (and set forth his reasons therefor in writing) that this requirement would prevent emergency restoration of the borrower's system or otherwise result in severe hardship to the borrower.

[(5) No loan shall be made in any State which now has or may hereafter have a State regulatory body having authority to regulate telephone service and to require certificates of convenience and necessity to the applicant unless such certificate from such agency is first obtained. In a State in which there is no such agency or regulatory body legally authorized to issue such certificates to the applicant, no loan shall be made under this section unless the Governor of the telephone bank shall determine (and set forth his reasons therefor in writing) that no duplication of lines, facilities, or systems, providing reasonably adequate services will result therefrom.]

(5) As used in this section, the term "telephone lines, facilities, or systems" shall mean lines, facilities, or systems used in the rendition of telephone service, as that term is defined in section 203(a) of this Act.

[(6) As used in this section, the term telephone service shall have the meaning prescribed for this term in section 203(a) of this Act, and the term telephone lines, facilities, or systems shall mean lines, facilities, or systems used in the rendition of such telephone service.]

[(7)] *(6)* No borrower of funds under section 408 of this Act shall, without approval of the Governor of the telephone bank under rules establshed by the Telephone Bank Board, sell or dispose of its property, rights, or franchises, acquired under the provisions of this Act, until any loan obtained from the telephone bank, including all interest and charges, shall have been repaid.

(c) The Governor of the telephone bank is authorized under rules established by the Telephone Bank Board to adjust, on an amortized basis, the schedule of payments of interest or principal of loans made under this section upon his determination that with such readjustment there is reasonable assurance of repayment: *Provided, however,* That no adjustment shall extend the period of such loans beyond fifty years.

SEC. 409. TELEPHONE BANK RECEIPTS.—Any receipts from the activities of the telephone bank shall be available for all obligations and expenditures of the telephone bank.

SEC. 410. CONVERSION OF OWNERSHIP, CONTROL AND OPERATION OF TELEPHONE BANK.—(a) Whenever fifty-one per centum of the maximum amount of class A stock issued to the United States and outstanding at any time after September 30, 1985, has been fully redeemed and retired pursuant to section 406(c) of this title—

(1) the powers and authority of the Governor of the telephone bank granted to the Administrator of the Rural Electrification Administration by this title IV shall vest in the Telephone Bank Board, and may be exercised and performed through the Governor of the telephone bank, to be selected by the Telephone Bank Board, and through such other employees as the Telephone Bank Board shall designate;

(2) the five members of the Telephone Bank Board designated by the President pursuant to section 405(b) shall cease to be members, and the number of Board members shall be accordingly reduced to eight unless other provision is thereafter made in the bylaws of the telephone bank;

(3) the telephone bank shall cease to be an agency of the United States, but shall continue in existence in perpetuity as an instrumentality of the United States and as a banking corporation with all of the powers and limitations conferred or imposed by this title IV except such as shall have lapsed pursuant to the provisions of this title.

[(b) When all class A stock has been fully redeemed and retired, loans made by the telephone bank shall not continue to be subject to the restrictions prescribed in the provisos to section 408(a)(2).]

[(c)] *(b)* Congress reserves the right to review the continued operations of the telephone bank after all class A stock has been fully redeemed and retired.

SEC. 411. LIQUIDATION OR DISSOLUTION OF THE TELEPHONE BANK.—In the case of liquidation or dissolution of the telephone bank, after the payment or retirement, as the case may be, first, of

all liabilities; second, of all class A stock at par; third, of all class B stock at par; fourth, of all class C stock at par; then any surpluses and contingency reserves existing on the effective date of liquidation or dissolution of the telephone bank shall be paid to the holders of class A and class B stock issued and outstanding before the effective date of such liquidation or dissolution, pro rata.

SEC. 412. BORROWER NET WORTH.—Except as provided in subsection (b)(2) of section 408, notwithstanding any other provision of law, a loan shall not be made under section 201 of this Act to any borrower which during the immediately preceding year had a net worth in excess of 20 per centum of its assets unless the Administrator finds that the borrower cannot obtain such a loan from the telephone bank or from other reliable sources at reasonable rates of interest and terms and conditions.

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